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EXTENSION OF AUTHORITY FOR PILOT PROJECTS FOR CONTRACT WITH PRIVATE ATTORNEYS FOR DEBT COLLECTION; AND DEBT COLLECTION AMENDMENTS ACT OF 1990

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HEARING

BEFORE THE

SUBCOMMITTEE ON ADMINISTRATIVE LAW AND GOVERNMENTAL RELATIONS

OF THE

COMMITTEE ON THE JUDICIARY
HOUSE OF REPRESENTATIVES

ONE HUNDRED FIRST CONGRESS

SECOND SESSION

ON

H.R. 4384

TO EXTEND UNTIL SEPTEMBER 30, 1992, THOSE PROVISIONS OF SECTION 3718 OF TITLE 31, UNITED STATES CODE, RELATING TO CONTRACTS FOR COLLECTION SERVICES

AND

H.R. 4535

DEBT COLLECTION AMENDMENTS ACT OF 1990

MAY 10, 1990

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EXTENSION OF AUTHORITY FOR PILOT PROJECTS FOR CONTRACT WITH PRIVATE ATTORNEYS FOR DEBT COLLECTION; AND DEBT COLLECTION AMENDMENTS ACT OF 1990

THURSDAY, MAY 10, 1990

House of Representatives,
Subcommittee on Administrative Law
and Governmental Relations,
Committee on the Judiciary,
Washington, DC.

The subcommittee met, pursuant to notice, at 10:14 a.m., in room 2226, Rayburn House Office Building, Hon. Barney Frank (chairman of the subcommittee) presiding.

Present: Representatives Barney Frank, Dan Glickman, Tom Campbell, Lamar S. Smith, Chuck Douglas, and Craig T. James.

Also present: Janet S. Potts, chief counsel; Belle Cummins, assistant counsel; Cynthia Blackston, chief clerk; and Roger T. Fleming, minority counsel.

Mr. Frank. The Subcommittee on Administrative Law and Governmental Relations will come to order and we will begin with our hearing on the question of debt collection.

A lot of our colleagues have been very interested in this issue. We have already acted on it once, when this subcommittee initiated some action a few years ago. This is both an oversight hearing and a hearing on two pieces of legislation that would continue and expand this practice.

[The bills, H.R. 4384 and H.R. 4535, follow:]

I

101st CONGRESS
2d Session

H. R. 4384

To extend until September 30, 1992, those provisions of section 3718 of title 31, United States Code, relating to contracts for collection services.

IN THE HOUSE OF REPRESENTATIVES

March 27, 1990

Mr. Frank introduced the following bill; which was referred to the Committee on the Judiciary

---

A BILL

To extend until September 30, 1992, those provisions of section 3718 of title 31, United States Code, relating to contracts for collection services.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. EXTENSION OF DEBT COLLECTION PILOT PROGRAM.

Section 5 of Public Law 99-578 (31 U.S.C. 3718 note) is amended by striking "a period" and all that follows through "4" and inserting "the period beginning on the date on which regulations become effective under section 4 and ending on September 30, 1992".

SEC. 2. CONFORMING AMENDMENT.

Section 6(a) of Public Law 99–578 (31 U.S.C. 3718 note) is amended by striking "3-year".

○

I

101st CONGRESS
2d Session

H. R. 4535

To amend chapter 37 of title 31, United States Code, with respect to debt collection by the United States.

IN THE HOUSE OF REPRESENTATIVES

April 18, 1990

Mr. Frank introduced the following bill; which was referred to the Committee on the Judiciary

---

A BILL

To amend chapter 37 of title 31, United States Code, with respect to debt collection by the United States.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the "Debt Collection Amendments Act of 1990".

SEC. 2. DEFINITIONS.

Section 3701(c) of title 31, United States Code, is amended by striking ", of a State" and all that follows through "local government".

SEC. 3. COLLECTION AND COMPROMISE.

Section 3711(a)(2) of title 31, United States Code, is amended by striking "$20,000 (excluding interest)" and inserting "$100,000 (excluding interest), or such higher amount as the Attorney General shall from time to time prescribe,".

SEC. 4. ADMINISTRATIVE OFFSET.

Section 3716(c) of title 31, United States Code, is amended—

(1) in paragraph (1), by striking "or" after the semicolon;

(2) in paragraph (2), by striking the period at the end and inserting "; or"; and

(3) by adding at the end the following new paragraph:

"(3) to a claim relating to a contract that is subject to the Contract Disputes Act of 1978.".

SEC. 5. INTEREST AND PENALTY ON CLAIMS.

Section 3717 of title 31, United States Code, is amended by adding at the end the following new subsection:

"(i) This section shall not prohibit the recovery of interest that has accrued on the outstanding debt before the notice required under subsection (b), if the recovery of such interest is otherwise permitted.".

SEC. 6. EXTENSION OF DEBT COLLECTION PILOT PROGRAM.

(a) EXTENSION OF PROGRAM.—Section 5 of Public Law 99–578 (31 U.S.C. 3718 note) is amended by striking "a period" and all that follows through "4" and inserting "the period beginning on the date on which regulations become effective under section 4 and ending on September 30, 1992".

(b) CONFORMING AMENDMENT.—Section 6(a) of Public Law 99–578 (31 U.S.C. 3718 note) is amended in the first sentence by striking "referred to in section 5" and inserting "beginning on the date on which regulations become effective under section 4".

○

Mr. FRANK. Mr. James.

Mr. JAMES. Thank you so much for appearing. We look forward to your testimony. I am afraid I will have to read most of it, because I have got a conflicting hearing. It is basically a noncontroversial issue, as I understand it and we are listening with very attentive ears and reading it with the expectation that we will proceed in a manner that you very much would like, I think, from the information that I have gathered.

Thank you so much for appearing. I will have to leave shortly to go to another hearing. Thank you.

Mr. FRANK. Thank you, sir.

Our first witness is Mr. Stuart Schiffer, of the Civil Division of the Justice Department, and Mr. Robert Ford, who is Deputy Assistant Attorney General for Debt Collection Management.

Gentlemen. If you will go first, Mr. Schiffer.

STATEMENT OF STUART E. SCHIFFER, DEPUTY ASSISTANT ATTORNEY GENERAL, CIVIL DIVISION, DEPARTMENT OF JUSTICE

Mr. SCHIFFER. Thank you, Mr. Chairman and Congressman James.

If I may submit my brief remarks, my brief printed remarks for the record, I will be even briefer in my summary.

Mr. FRANK. Without objection.

Mr. SCHIFFER. We are grateful to the subcommittee for holding this hearing this morning. I think debt collection is an extremely important topic. We are especially grateful to the chairman for introducing H.R. 4535. I will, in the main, confine my summary remarks to H.R. 4535.

Preliminarily, though, I did want to emphasize how proud we are in the Department of what we regard as very significant and constantly increasing success we have been enjoying in the collection area. The numbers are sometimes hard to get hold of, but they are rising and are rising at a very increasing rate, as they should be.

My colleague on my left, Mr. Ford, maintains one set of numbers which is really the set I favor, because it is the most specific and it is the toughest to argue with. Mr. Ford keeps track of actual dollars collected by the litigating divisions and U.S. attorneys, because cash is something you cannot argue about.

The numbers that Mr. Ford showed me yesterday indicate that the Civil Division, for example, where I labor, has collected in the first half of this fiscal year over $109 million. I take special pride in that number, because the budget for the entire Civil Division is something on the order of $102 million. When we consider that, the last time I looked, about 15 percent of our caseload is in the affirmative area, so that all of the rest of our resources are devoted to defending suits against the Government. I think it is a remarkable achievement to have brought in already an amount so far in excess of our budget for the entire year for all of our litigation.

Other components of the Department, especially the U.S. attorneys, have similar records. I think as we sit here, the Department has brought in, again, in cash, something approaching $300 million at this stage in the fiscal year.

I emphasize that is cash only, because while other recoveries are sometimes tougher to measure, there are many recoveries we achieve which have cash equivalence, when we foreclose on property or have property returned to an agency.

You are going to hear from the Department of Agriculture after we are through, but in certain agriculture programs alone, such as programs administered by the Rural Electrification Administration, we have had literally billions of dollars at issue in loans that were either in default or verging on default, and in many of those, working closely with the Department of Agriculture, we have achieved workout agreements that have taken what appeared to be woeful situations and ended up with viable workout agreements. That is not counted in the cash numbers, but as these loans become current again and get repaid, they are certainly very much additional recoveries.

H.R. 4535, which the chairman introduced, is not intended to be a panacea for all of our problems, and I equally do not assume that it is going to provide an immediate surge in recoveries. Nevertheless, I think it is very needed and very sound legislation. Its purpose is principally interpretive, to remove what we perceive as unnecessary and we think unintended obstacles to collection of at least certain classes of claims.

The first thing the bill would do would be to raise the general authority of Government agencies, absent some other specific authority, to compromise or close claims from its present ceiling of $20,000 to $100,000, and to authorize the Attorney General, from time to time, to adjust that figure.

The current $20,000 figure dates back to the 1966 Federal Claims Collection Act. It has become thoroughly outmoded. It should have been adjusted years ago. As we indicated in our prepared testimony, many of the claims that presently fall between $20,000 and $100,000 simply lead to what we see as needless paper-shuffling between agencies and the Department.

The questions typically presented in these cases are not of legal moment, but they are really analyzing financial forms to ascertain, indeed, whether claims are collectible and in what amount. We find that in this area we rarely disagree with client agencies. Inflation alone would call for a marked upward adjustment to let us concentrate on the larger cases.

Second, the bill is intended to make clear that the 1982 Debt Collection Act was not intended to abrogate the Government's historic right to offset and to charge interest on claims against States and local governmental units. The 1982 act was intended to facilitate Government debt collection, not to make it more difficult, and yet we have at least some courts who have held that the Government, as the result of what they see as certain specific wording in the act, can no longer utilize offset or can no longer charge interest to States and to local governments.

We are very mindful of the financial plight that States, in general, certain States specifically, and local governments find themselves in from time to time, and yet we think if Congress has not chosen to forgive certain indebtedness or to couch programs as grants, instead of loans, it behooves us to at least have the tools to collect. When an overdue loan is essentially interest free, it almost does not make business sense for the debtor to make repayment. We think we must be able to charge interest and we must be able to use the offset right, and what we are seeing now, instead, is needless litigation. We have at least——

Mr. FRANK. I think we cover that point in the act.

Mr. SCHIFFER. OK.

Mr. FRANK. I appreciate when people say they are going to summarize their statement, instead of read it, but I must tell you, almost always that turns out to be longer than if the statement is read, so I would encourage you to just—we have got the point, I think.

Mr. SCHIFFER. Two more minutes and I will be done.

The next thing the bill would do would be to overturn a decision of the Armed Services Board of Contract Appeals, which held that the Gcvernment had to follow certain procedures specified in the Debt Collection Act, before it can offset claims against Government contractors.

There is a separate very specific regime stated in the Contract Disputes Act of 1978 which defines the means by which disputes between the Government and its contractors should be resolved. We do not believe there was any intent to engraft yet an additional set of procedures in the Debt Collection Act. This bill would make clear that the Contract Disputes Act procedures govern the debt collection procedures.

Finally, section 5 of the bill, the last section on which I need comment—my colleague will talk about the pilot project—is simply meant to clarify the intent of the Debt Collection Act regarding how interest is to be charged on certain loans.

The Debt Collection Act mandated that the agencies charge interest, something, remarkably enough, some agencies were not doing, and it specifies that interest is to run from the date the agency makes demand or sends a demand notice. We do not think that was intended to change the rule that the Government and other creditors historically were able to charge interest as an element of certain debts, from a date that might have antedated the demand.

In a fraud case, for example, the rule has always been that interest runs from the time that the diversion occurs, that the fraudulent act occurs. We do not think that Congress meant that the charging of interest had to await a demand letter. It is just another clarification.

With that, I will simply again endorse H.R. 4535 and pledge our renewed commitment to what the taxpayers have a right to demand, collection of amounts owing the Government, and let my colleague proceed.

Thank you.

Mr. FRANK. Thank you.

[The prepared statement of Mr. Schiffer follows:]

PREPARED STATEMENT OF STUART E. SCHIFFER, DEPUTY ASSISTANT ATTORNEY GENERAL, CIVIL DIVISION, DEPARTMENT OF JUSTICE

Mr. Chairman and Members of the Subcommittee:

We appreciate the opportunity to set forth our views on H.R. 4535, the "Debt Collection Act Amendments of 1990." We urge that the bill be enacted.

The bill would amend the Federal Claims Collection Act to allow agency heads to compromise, terminate, or suspend collection action on claims up to a maximum amount of $100,000, subject to further increases at the discretion of the Attorney General. The present statute allows such action by agency heads only up to a maximum amount of $20,000, a figure which has been unchanged since 1966. The higher figure is appropriate to take into account the effects of inflation and to avoid needless internal government review of relatively small claims.

It is estimated that the effect of inflation alone from 1966 to 1990 would indicate that the $20,000 limit on agency compromise authority should be raised to $70,000. Because the limit has not been raised over the years, the Civil Division of the Department of Justice must now process many claims, particularly benefit overpayment claims from the Social Security Administration, the Department of Veterans Affairs disability and housing programs, and the Department of Labor Black Lung program in the $20,000 to $50,000 range. The Civil Division almost always approves compromise or termination of the claims based on the agency's investigation of the debtor's ability to pay. There are almost never any legal issues or other matters which would require an extensive analysis of the claim by the Civil Division. On the other hand, it is often important to the debtors, who are often ill or elderly, that a resolution of the Government's claim against them be processed as quickly as possible.

Raising the limit on agency compromise and termination authority from $20,000 to $100,000 would not only diminish needless paper-shuffling and time in processing these claims between the affected agency and the Department of Justice, it would also free scarce resources both in the agency and the Civil Division to concentrate on larger claims in order to ensure that the Government's interests are protected by giving closer scrutiny to such claims.

Section 2 of the bill would amend the Debt Collection Act of 1982 to affirm that the Act was not intended to abrogate the Government's right of offset and to recover interest against a state or local government. Several appellate courts have held that the exclusion of state and local governments from the definition of "person" in the Act, 31 U.S.C. §3701(c) meant that Congress abrogated the Government's historic common law right to collect interest on debts owed by state and local government. Without this bill, these decisions could also be extended to the Government's common law right to offset monies owed state and local governments against debts owed by them.

Prior to the Debt Collection Act of 1982, there was little doubt that the Government could collect interest on debts which were owed to it by state and local governments. West Virginia v. United States, 479 U.S. 305 (1987). Similarly, the United States, like any other creditor, has long asserted a common law right to offset its claims against monies owed by it to a debtor. United States v. Munsey Trust Co., 332 U.S. 234 (1947). When the Debt Collection Act of 1982 set forth certain procedures to be followed in charging interest, 31 U.S.C. §3717, and offsetting claims, 31 U.S.C. §3716, the definition of "person" in 31 U.S.C. §3701 excluded state and local governments from the application of those provisions. The Government took the position, however, in the Federal Claims Collection Standards ("FCCS") which implemented the Debt Collection Act, that the Government retained the common law right both to charge interest and to offset debts against state and local governments. 4 C.F.R. §§102.3(b)(4) and 102.13(i)(2).

Subsequently, certain appellate courts held that the Debt Collection Act abrogated the Government's common law right to charge interest against state or local governments. See, e.g., Arkansas v. Block, 825 F.2d 1254 (8th Cir. 1987); Commonwealth of Pennsylvania v. United States, 781 F.2d 334 (3d Cir. 1986); Perales v. United States, 598 F. Supp. 19 (S.D.N.Y.), aff'd, 751 F.2d 95 (2d Cir. 1984) (per curiam). Contra Gallegos v. Lyng, 891 F.2d 788 (10th Cir. 1989) (holding that Act did not abrogate Government's common law right to charge interest against states).

H.R. 4535 is intended to eliminate further confusion about the continued viability of the Government's rights to charge interest and to offset in cases where state and local governments owe money. Because of the general immunity of such governments from most usual forms of debt collection such as foreclosure on property or garnishment, the Federal Government's ability to charge interest and to offset are often the most effective methods of ensuring payment by recalcitrant state and local government debtors. Without these debt collection tools, the Government's ability to enforce debt collection against state and local governments would be substantially impaired.

Section 4 of this bill would overturn a decision of the Armed Services Board of Contract Appeals, DMJM/Norman Engineering Co., ASBCA No. 28154, 84-1 BCA 17,226 (1984), which held that the Government must follow the procedures set forth in the Debt Collection Act of 1982, 31 U.S.C. §3716, before using its common law right of offset to collect amounts due from government contractors. As indicated above, this right of offset has historically been used by the Government and has never been challenged.

However, since the Norman Engineering decision, government contractors have argued that, before effecting an offset, the Government must follow the administrative offset provisions established in the Debt Collection Act, 31 U.S.C. §3716. These include: (1) notice of the claim and the intention to offset; (2) "an opportunity to inspect and copy the records of the agency related to the claim;" (3) an opportunity to review an agency's decision relating to the claim; and (4) an opportunity to make a written agreement with the agency on the terms of repayment. Contractors could make particular use of this theory to demand access to all records relating to the contract, in effect using it as a right of discovery.

We do not believe that the Debt Collection Act procedures governing offset were intended to apply to traditional contract disputes which are governed by the Contract Disputes Act of 1978, 41 U.S.C. §601 et seq. Under these disputes procedures, a contractor may request a Contracting Officer's decision on any dispute with the Government concerning a contract; review from such a decision may be had either in an agency board of contract appeals or the United States Claims Court. There is nothing in the Debt Collection Act which indicates that Congress intended to displace the disputes procedures traditionally covering Government contracts when the dispute concerned the Government's offset of monies against a contractor. H.R. 4535 would ensure that the Debt Collection Act does not hinder Government efforts to collect money owed to the Government because of inadequate contract performance.

Section 5 of the bill would amend 31 U.S.C. §3717 by adding a new subsection to clarify the intent of the Debt Collection Act regarding how interest is charged on delinquent debt. The Debt Collection Act was intended by Congress to compel agencies to adopt more forceful policies in collecting debts owed the Government. Prior to passage of the Act, many agencies were not actively pursuing repayment of overdue debt and, contrary to sound credit practices, were not charging delinquent debtors interest on overdue debts despite demands from the agencies for repayment. To remedy this practice, Congress directed agencies to charge interest from the date that they send a demand letter to a debtor.

The Debt Collection Act was not intended, however, to define the elements or components of a debt, which are determined under established principles of law pertaining to the particular debt in question. The statutory direction in the Debt Collection Act that agencies were to charge interest on debt from the date of the demand letter was not intended to foreclose recovery of interest in cases where applicable law considers interest as an element of the underlying debt.

H.R. 4535 clarifies the Debt Collection Act by allowing the Government to recover interest prior to the date a demand letter is sent if such interest would otherwise be charged according to applicable law. This would often be the case, for example, where the debt arose as a result of fraudulent acts or misuse of federal monies. Under the common law, a private party under similar circumstances could recover that loss in the form of interest from the date of the diversion to the date that full restitution is made. This bill makes it clear that the common law would also be applicable to a debt owed the Government, and that interest would not be limited to the date the first demand letter is sent.

The final Section 6 of the bill would extend the three-year private counsel pilot project in the Federal Debt Recovery Act of 1986 from three to five years. My colleague, Deputy Assistant Attorney General Robert N. Ford, will address that portion of H.R. 4535, and H.R. 4384.

Thank you for this opportunity to present our views. I would be happy to respond to questions.

Mr. FRANK. Mr. Ford.

STATEMENT OF ROBERT N. FORD, DEPUTY ASSISTANT ATTORNEY GENERAL FOR DEBT COLLECTION MANAGEMENT, JUSTICE MANAGEMENT DIVISION, DEPARTMENT OF JUSTICE

Mr. FORD. Thank you, sir.

Mr. Chairman, I would too like to submit my statement and make it very brief, and I will indeed make it brief.

Mr. FRANK. Without objection.

Mr. FORD. I think one thing is important to address right at the beginning. I am sure the Chair is aware that the President submitted legislation in his budget, a supplemental piece of legislation that would extend the program.

Mr. FRANK. Let me say, with regard to extension, it is in the supplemental, it is in both branches. Should that get held up, I will talk to the chairman and I will ask the chairman's staff, if necessary, I would ask, since we are having a hearing, we might bring this out on a suspension. We are not going to let that get held up. I assume the supplemental will get passed before that. But if we get to a point where the supplemental appears to be held up, we would plan to move with a suspension of the rules on a quick extension of the time, so that we are not under that gun.

Mr. FORD. I appreciate that very much, Mr. Chairman. As I understand, yesterday the conferees met and agreed to meet again next Tuesday.

My part of this is, of course, the pilot project. We have since late 1987, late 1986, I guess, trying to run a pilot project in 10 judicial districts, pursuant to the Federal Debt Recovery Act. We contract with private counsel—the statute said we had to contract with four private counsels in each district—and we have contracts up and running and a system running now in six Federal judicial districts. We are running in Detroit, in Brooklyn, in Houston, in Miami, Los Angeles, the District of Columbia, and we will be running in July in San Francisco. These are districts that were picked primarily because the U.S. attorneys offices in those districts had large backlogs of cases that they did not have the resources to collect and enforce vigorously.

The private counsel contracts have been let. I have some figures which show that, as of yesterday, in fiscal 1990 we have sent a total of 822 new debts to the private counsel for collection, with a referred value of just under $5 million. In fiscal 1990, through yesterday, the private counsel had collected $838,343. There were pending with private counsel 4,652 cases, with a balance of $24 million.

I think everybody has been disappointed in the time that it took us to get the private counsel program going. We had, unfortunately, to follow the regular Government procurement laws, we had to go through a lot of lengthy contract procedures, and we had a protest that held us up. But now we are running and I think we are showing some good results.

Private counsel unanimously criticized the program for the lack of volume. They keep reading statements issued here in Washington that say there are $32 billion, or whatever number you might want to hear, of delinquent uncollected civil debt out there, and they wonder, if that is so, how come we have only been able to get 822 cases to them.

I do not know how good the $32 billion number is, but in any event, assuming that it is good, it is nationwide. We are only dealing with some specific pilot districts. Obviously, though, from the ones I mentioned, they are major metropolitan areas, so we would think there would be a significant number in those districts.

In fiscal 1989, we got only 1,434 new cases, referred to us from all Federal agencies for our pilot districts. This year, we have already surpassed that. So, we think now that we have the first five districts up and running, this fiscal year we will complete, I hope, installation of the next five pilot sites. Then, with the extension, we would have 2 years to do no more installations and just collect data and see what information we could bring to the Congress, so that you could determine whether you want private counsel to become a permanent part of the debt collection arsenal of the Government.

Thank you.

Mr. FRANK. Thank you.

[The prepared statement of Mr. Ford follows:]

PREPARED STATEMENT OF ROBERT N. FORD, DEPUTY ASSISTANT ATTORNEY GENERAL FOR DEBT COLLECTION MANAGEMENT, JUSTICE MANAGEMENT DIVISION, DEPARTMENT OF JUSTICE

Mr. Chairman and Members of the Subcommittee:

It is a pleasure to be here to testify about the private counsel debt collection pilot project.

With your permission, Mr. Chairman, I have a brief prepared statement to which I have attached a comprehensive outline of our progress in the pilot project, and I offer these for the record. I can summarize what is in the statement and outline, and then I shall be happy to try to answer any questions you or the members of this Subcommittee may wish to ask.

Before I turn to the pilot project, if I may, by way of background and introduction, I would like to paint a brief portrait of the role of the Department of Justice in the Government's credit management and debt collection picture.

Stated succinctly, the Department of Justice is the Federal Government's collector of last resort. In carrying out this function, the Department plays a dual role. First, we collect the criminal fines, penalties, and civil debts which are awarded by the courts as the result of litigation conducted by the 93 U.S. Attorneys, their Assistants, and the other lawyers in the Department's six litigating divisions--the Antitrust Division, the Civil Division, the Civil Rights Division, the Criminal Division, the Land and Natural Resources Division, and the Tax Division.

Second, we sue delinquent debtors on behalf of our various Federal Agency clients to collect debts these agencies have been unable to collect with techniques short of litigation. As the members of this Subcommittee are well aware, it seems that almost every Federal Agency has some programs for lending money directly to people or companies, or pursuant to which they guarantee loans made to people or companies by financial institutions in the private sector.

When these loans go into default, the Federal Agencies try to collect what they are owed from the debtors. Frequently, these Federal Agencies even enlist the aid of private sector collection agencies to help collect these delinquent debts.

Unfortunately, some debtors are recalcitrant, and they refuse all entreaties to pay their Federal obligations. Eventually, the Federal Agencies reach the point where they realize that if the Government is ever going to recover anything from these deadbeats, it will have to sue them. At this point, Justice sues these debtors to collect the delinquent debts they have refused to pay.

Actually, the process is similar to what happens in the private sector. There, when one defaults on a debt and declines to pay in response to dunning by the creditor, and perhaps even a debt collection agency, if enough money is involved, the creditor will eventually send the debt to a lawyer with instructions to sue the debtor to collect the debt.

We, at the Department, are proud of the job we have done in these two roles over the past few years. For example, we started keeping data on the cash we collect from suing debtors in Fiscal 1982, and from that time through the end of March 1990, we have returned over $3.4 billion, in cash, to the United States Treasury.

Most of this money has been collected by the U.S. Attorneys because they handle most of the Department's litigation and get most of the cases referred from our client Federal Agencies. In fact, in Fiscal 1989, the U.S. Attorneys collected and deposited in the Treasury a total of $311,504,407--in cash--a sum that represents almost 68 cents for every single dollar of the $460,212,000 appropriated by the Congress to fund all of the U.S. Attorneys' operations that year.

However, more can be done, and that brings us back to the pilot project. The basic purpose of the pilot is to determine whether using private attorneys to handle a portion of our debt collection activity as a supplement to Justice resources, will be beneficial in terms of both more timely and increased collections. As set forth in the attached outline, we have made significant progress in the pilot project. In addition, we have created a new automated debt tracking and collection system which we named "COLLECTOR." We have "COLLECTOR" installed and operating in 6 Federal judicial districts, and expect to have it up and running in all 10 of the pilot districts before the end of this fiscal year. Once it is in place nationally, "COLLECTOR" will greatly improve the Department's ability to track all debt collection cases at Justice.

Our main problem now is that the Attorney General's authority to continue the pilot expires on September 1, 1990.

Accordingly, the President, in the Fiscal 1990 Supplemental section of his Fiscal 1991 Budget request, and the Attorney General in his annual report on the pilot project, requested legislation extending it through September 30, 1992. H.R. 4384 and H.R. 4535 would accomplish this goal and we support their prompt enactment. The identical extension also is included in H.R. 4404, the Supplemental Appropriation legislation. This extension should give us time to collect sufficient data for an informed evaluation of the pilot project's results.

This concludes my prepared statement. I shall be happy now, Mr. Chairman, to try to answer any questions you or any members of the Subcommittee may wish to ask about the pilot project.

PRIVATE COUNSEL PILOT PROGRAM

BACKGROUND

o The Federal Debt Recovery Act (FDRA) was enacted as part of a comprehensive program to improve the Federal Government's credit management and as one of the Administration's privatization initiatives.

o The pilot program required by the FDRA enlists the aid of private counsel in pursuing debtors who are reported by Federal agencies to owe the Federal Government some $32 billion in non-tax delinquent debts.

o The FDRA empowers the Attorney General to:

- Conduct competitive procurements and enter into contracts with at least four private law firms in five to ten judicial districts as a pilot program to evaluate whether enhancing the Government's debt collection resources with private counsel will increase Federal debt collection receipts.

- Pay private counsel who win the debt collection contracts a percentage of what they collect as a fee.

o In addition, the FDRA requires the Attorney General to:

- Submit a detailed annual report to the Congress on the results of the pilot program.

- Use his "best efforts" to contract with some "small and disadvantaged" law firms to enable such firms to receive about 10% of the Federal Government's debt collection business.

o The three year life of the FDRA began sixty days after the Attorney General sent the Congress the regulations he promulgated pursuant to the Act on August 31, 1987. Therefore, the Act will expire on September 1, 1990.

STEPS TAKEN TO IMPLEMENT THE FDRA

o Selected the following five districts which have large backlogs of uncollected debts as the first pilot districts:

Eastern District of New York (Brooklyn)
Southern District of Florida (Miami)
Eastern District of Michigan (Detroit)
Southern District of Texas (Houston)
Central District of California (Los Angeles)

(4/16/90)

- o Conducted an extensive publicity campaign in five pilot districts to reach out to large and small firms and encourage widest possible participation.

- o Result was over 1,000 requests from sole practitioners and small, medium, and large law firms of every description for copies of our Request for Proposals (RFP) so they could decide whether to bid for our contracts.

- o Eighty-five (85) firms eventually bid on our debt collection contracts--more bids than the Department had ever received on any procurement--distributed as follows:

DISTRICT	REQUESTS FOR RFPs	PROPOSALS RECEIVED
Brooklyn, N.Y.	192	20
Miami, Florida	281	19
Detroit, Michigan	205	16
Houston, Texas	95	12
Los Angeles, Calif.	404	18
TOTAL	1,177	85

- o Competitive procurement process took one year. Negotiations with firms in all five pilot districts finally completed and contracts awarded to 4 firms in each pilot district.

- o The 20 firms submitted bids ranging from 10% to 38% as their fees for handling Federal debt collection litigation.

- o In implementing the Attorney General's responsibility under the FDRA to "use his best efforts to enter into [debt collection] contracts . . . with law firms owned and controlled by socially and economically disadvantaged individuals . . . ," our outreach program and the competitive procurement process combined to ensure that we met the statute's objectives.

- o Detroit selected as first district to get pilot program because former U.S. Attorney--Roy C. "Joe" Hayes--was Chairman of the Debt Collection Subcommittee of Attorney General's Advisory Committee of U.S. Attorneys, and he has been exemplary in cooperating with Department personnel charged with implementing the pilot.

- o The first debts sent to private counsel for collection were from a pool of backlogged cases in which the U.S. Attorneys' debt collection units had obtained judgments against the debtors but did not have the time and resources to pursue actively to enforce the judgments.

(4/16/90)

- After the initial backlog is distributed to private counsel, they will receive four out of every five pilot program civil debts referred to the pilot Districts for collection by the Department of Education, the Veterans Administration, the Small Business Administration, the Department of Housing and Urban Development, or any other Federal agency with recalcitrant debtors who have refused to pay without being sued. The fifth debt referred, on a rotating basis in each pilot district, will go to the U.S. Attorney's Office for litigation.

- Therefore, the addition of four private counsel in each of the pilot districts gives the Government five law firms to sue debtors in each pilot district [4 private firms plus the U.S. Attorney] instead of the single firm [the U.S. Attorney] it had before.

- Selected the following second five pilot districts:

  District of New Jersey (Newark)
  District of Columbia (Washington, D.C.)
  Middle District of Georgia (Macon)
  Middle District of Florida (Tampa)
  Western District of Louisiana (Shreveport)

- Four of these districts--all except the District of Columbia--were selected primarily because they have large backlogs of foreclosures pending under the Rural Housing Program administered by the Farmers Home Administration (FmHA) of the United States Department of Agriculture (USDA).

- Macon has since been dropped from the pilot because of a decision by the Eleventh Circuit which may permit FmHA to use Georgia's non-judicial foreclosure procedures in that state.

- Northern District of California (San Francisco) selected as tenth pilot site to replace Macon. Process of selecting lawyers and law firms in this district is now underway.

- Project implemented in Detroit on October 11, 1988; in Brooklyn on March 6, 1989; in Houston on May 8, 1989; in Miami on July 17, 1989; in Los Angeles on September 25, 1989; and in Washington, D.C. on April 16, 1990.

(4/16/90)

- The following data show the number of law firms in each of the second five pilot districts which requested a copy of our RFP and the number of firms sent RFPs which submitted proposals:

DISTRICT	REQUESTS FOR RFPS	PROPOSALS RECEIVED
New Jersey	65	5
Washington, D.C.	100	6
Macon, Georgia	78	4
Tampa, Florida	70	5
Shreveport, Louisiana	118	11
TOTAL	431	31

- Started process to select private counsel in second five pilot districts by initial evaluation of responses to RFP during last week of April 1989 and conducted interviews with potential private firms during May and June 1989.

- Attorney General announced awards of contracts to private counsel in Newark, New Jersey; Washington, D.C.; Tampa, Florida; and Shreveport, Louisiana on September 18, 1989.

- Firms which won contracts in these four districts submitted bids ranging from 18.5% to 29% for collecting unsecured debts and flat rates for foreclosures of from $125 to $1,000 each.

OTHER RELEVANT GENERAL DATA

- The FDRA exempts debts arising under the Internal Revenue Code, the Social Security Act, and the tariff laws from those which can be sent to private counsel for litigation.

- An AUSA in each pilot district will monitor private counsels' debt collection litigation and be responsible for all fundamental decisions, including whether to initiate litigation and whether to compromise or settle a claim.

- Initially, we have determined not to send criminal fines or debts of over $25,000 to private counsel for litigation.

- As a compromise between those who argued for giving private counsel maximum flexibility in selecting the courts in which to sue Federal debtors and those who would restrict private counsel to suing only in Federal district courts, we decided to permit private counsel initially to sue on debts of up to $10,000 in local, state, or Federal courts at their option, but require all suits on debts over $10,000 to be brought in U.S. District Courts.

(4/16/90)

CENTRAL INTAKE FACILITY

- o Client agencies used to refer all debts for litigation directly to the U.S. Attorney in whose district the debtor resides. In effect, we have debts coming to the Department through 94 different doors and we never have accurate and current data on the number of debts sent to us or their value. The Department's debt collection management people believe that replacing these 94 doors with a single door--a Central Intake Facility (CIF)--will solve many of our basic debt collection problems. OMB agrees, and together we decided to use the FDRA pilot program to also test the central intake concept.

- o The CIF is not required by the FDRA, but it is essential if the Department is to be able to keep track of debts referred to private counsel and the U.S. Attorneys in the pilot districts and compile the statistics necessary to report to the Congress as the FDRA mandates.

- o The CIF is run by a private contractor with appropriate computer capability. It automates the following functions, many of which we were not now able to accomplish in a timely manner, if at all, before it opened:

  - Receive debts sent by Federal agencies for enforced collection, via litigation by pilot district U.S. Attorneys and private counsel.

  - Screen all incoming debts to ensure they are suitable for litigation. (For example, that the statute of limitations has not run.)

  - Return defective cases to referring Federal agencies or acknowledge receipt of appropriate cases to the referring agencies and let them know which of their cases are sent to the U.S. Attorneys and which to specified private counsel.

  - Act as a central data bank of referred debts so we will, for the first time, know how many debts we have received from each agency and the value of such debts.

  - Electronically transfer essential data on each debt to the pilot district U.S. Attorneys and the private counsel with whom we have contracts.

  - Receive all payments collected by pilot district U.S. Attorneys and private counsel and deposit them daily into the appropriate accounts in the Treasury.

(4/16/90)

- Produce automatically all pleadings, letters, and other litigation documents required by the pilot district U.S. Attorneye and private contract counsel.

- Create automated reporte to inform our client agencies monthly of the dollare collected on their cases and prepare periodic statue reports on the progress of our casee for the Department and our client agencies.

- Compute monthly the amount of fees we are obligated to pay private counsel in the pilot districts on the basis of the amounts they collect and notify Treasury to send private counsel checks in the appropriate amounts.

- Compute automatically the data we need to reconcile our accounte with our client agencies, create the proper audit traile for the GAO audits the FDRA calls for, and prepare the reports the FDRA requires be submitted to the Congrees.

o The CIF contractor will aleo inetall in each U.S. Attorney's and private couneel's office in the pilot districte the latest computer equipment and eyetems to enable us to evaluate new debt collection technology.

o On August 22, 1988, all of our client agencies etarted sending their debte for litigation in our first five pilot districts to the CIF instead of sending them directly to the pilot district U.S. Attorneye.

o Starting October 1, 1988, the CIF took on the task of referring all new collection cases from various Federal agencies to the appropriate pilot district U.S. Attorneys.

o On October 11, 1988, we switched on our automated system- "COLLECTOR" - in the officee of the U.S. Attorney and four private law firms in Detroit and all five sites were then connected to our CIF in Silver Spring, Md.

o On March 6, 1989, we took "COLLECTOR" to the U.S. Attorney in Brooklyn and four private firms in the Eastern District of New York.

o On May 8, 1989, we took "COLLECTOR" to the U.S. Attorney in Houston and four private firms in the Southern District of Texas.

(4/16/90)

- On July 17, 1989, we took "COLLECTOR" to the U.S. Attorney in Miami and three private firms in the Southern District of Florida.

- On September 25, 1989, we took "COLLECTOR" to the U.S. Attorney in Los Angeles and three private firms in the Central District of California. We now have all of the first five pilot sites automated.

- On December 4-7, 1989, we met with representatives in the first five pilot districts U.S. Attorneys' and private counsel offices to discuss the pluses and minuses of the program.

- On April 16, 1990, we took "COLLECTOR" to the U.S. Attorney in the District of Columbia and three private firms in Washington, D.C.. We are scheduled to implement "COLLECTOR" in San Francisco, California in June 1990.

- The pilot program is also to be implemented in the Western District of Louisiana, the Middle District of Florida, and the District of New Jersey. In these districts, the main caseload is expected to be foreclosure cases for FmHA. We are working as fast as we can to develop automation to monitor foreclosure cases in these three districts.

(4/16/90)

Mr. FRANK. A couple of questions. For the first fiscal year that we have completed results, what is the ratio of collections to expenditures?

Mr. FORD. Well, I do not have the ratio in my mind, but I can——

Mr. FRANK. What were the numbers?

Mr. FORD. I can give you the numbers.

Mr. FRANK. If they are really big, we can probably——

Mr. FORD. The budget number we had for fiscal 1988 was $1.35 million. That included four people who were running the——

Mr. FRANK. How much have we collected?

Mr. FORD. The collections for that year were zero, because we did not get the system up and running in the first pilot site—Detroit—until October 11, 1988.

Mr. FRANK. This is fiscal 1989 or——

Mr. FORD. Fiscal 1988.

Mr. FRANK. No, I asked about——

Mr. FORD. For fiscal 1989, our budget for the pilot was $2.2 million, and for fiscal 1989, the private counsel collected—pardon me while I get to the number——

Mr. FRANK. Obviously, when we evaluate it, I think that is going to be the major——

Mr. FORD. I understand where the chairman is going, but in fiscal 1989, private counsel were referred 14 million dollars' worth of debts. They collected $174,445, but I do not think it is a true picture, because we brought them on seriatim through the year. The last of the private counsel, for example, was Los Angeles, and it did not get implemented until September of the fiscal year.

Mr. FRANK. Fine. Let me ask you a couple more questions. One thing we may be finding out is that some of this data is not as collectable as we think it is, and that would be one of the issues that I assume—$14 million referred and $174,000 collected. Is much of the rest of that still in litigation, or is much of the rest—any estimate of how much we decided we could not get and how much of it was still in litigation?

Mr. FORD. Well, let me try to clear this up, when I say in litigation. Basically——

Mr. FRANK. Not in litigation, in process, in discussion.

Mr. FORD. Basically, we get mostly default judgments, and so it is not contested litigation.

Mr. FRANK. I understand.

Mr. FORD. As of yesterday, the figures I have from our central intake facility, private counsel had, as I say, 4,652 cases pending in the——

Mr. FRANK. If you do not know the answer, please tell me. I understand that.

Mr. FORD. I am sorry, I may have misunderstood your question.

Mr. FRANK. The question was—you said $14 million was referred and $174,000 was collected. Now, I just want to know how much of that we had to write off as just uncollectable or unlikely to be collected—maybe we cannot say exactly—and how much of that is still in active collection proceedings.

Mr. FORD. Some of those numbers are in the annual report, Mr. Chairman, that we presented pursuant to the statute, and it showed that in fiscal 1989, for example, that the total debt closed, not collected, by both the pilot district U.S. attorneys and private counsel is $14,527,198. So, out of what was referred there, $14 million, in that fiscal year was closed as uncollectable. Undoubtedly, more of it will be closed this fiscal year as uncollectable.

Mr. FRANK. I thought $14 million was the total amount referred.

Mr. FORD. No sir, what I meant to say was that the amount of debt referred to private counsel alone in fiscal 1989 was $14 million.

Mr. FRANK. Yes, I thought in fiscal 1989, you said the budget was $2.2 million, and I thought $14 million was the total amount that was referred.

Mr. FORD. No, sir. If I said that, I misspoke. I am sorry. The amount of debt referred to private counsel alone in fiscal 1989 was $14, but they had also got some referred in fiscal 1988 that were out there and additional debts were referred to the pilot district U.S. attorneys.

Mr. FRANK. How much was referred before that?

Mr. FORD. The total referred to both private counsel and the U.S. attorneys in the first five pilot districts through the end of fiscal 1989 is $147,189,747.

Mr. FRANK. The reason I want to ask you that is I want to get some sense of—if we are writing off almost all of what we refer, then the thing does not work.

You said those figures are all in the report and I guess I can look at it, but it is those kinds of numbers that I think we are going to be—ultimately, I think this is going to rise or fall on those numbers, in terms of where we are.

Am I correct in assuming that, given, particularly in the pilot project, the state of the U.S. attorneys offices, very little of these debts would have been pursued absent the pilot project? Is that accurate?

Mr. FORD. I suspect that is true if they had not gotten an increase in resources.

Mr. FRANK. Yes. Well, given what they had.

Mr. Schiffer, do you have any comment on that?

Mr. SCHIFFER. I guess I am not prepared to say.

Mr. FRANK. OK.

Mr. SCHIFFER. The U.S. attorneys numbers, as indicated, are rising at a remarkable clip, so it is not fully clear to me. I think we need to evaluate the project.

Mr. FRANK. Agreed. That is why we are here.

When we first did this, we ran into a kind of unhappiness on the part of the Justice Department, to some extent, with the notion of going more to private counsel. Is that still a concern? Do you think, everything else being equal, we should not do it or should do it, or what?

Mr. SCHIFFER. No, I think unhappiness is too strong a word to describe my feelings. I have simply been guilty of being candid and confessing my parochial bias. I have spent too many decades at the Justice Department, so I have—do I have a feeling that the Justice Department does things more efficiently than the rest of the world? Yes, but I equally have a—you know, reality is we cannot be all things everywhere. We need help and we are not going to get——

Mr. FRANK. I hope you are kidding.

Mr. SCHIFFER [continuing]. And so I do not think——

Mr. FRANK. I hope you are kidding. I hope you are not saying that, you know, every institution has a bias. The purpose of public policy is to try and avoid that and it may very well be that, institutionally, that there are different roles that U.S. attorneys will, with a limited number of hours in a day and people, there may be better things for U.S. attorneys to do with their authority, with their backup, et cetera, et cetera, than simply pursuing bad debt, so I do not——

Mr. SCHIFFER. Absolutely, and I think that is why there has been unanimous administration support for this program.

Mr. FRANK. Let me ask one other question and then I will ask my colleague if he has any questions. The procurement practices you talk about, do we do competitive bidding on this?

Mr. FORD. Yes, sir.

Mr. FRANK. By price?

Mr. FORD. Yes, sir.

Mr. FRANK. What was the experience?

Mr. FORD. We got bids ranging from a low of 15 percent as a contingency fee to a high of 33.3 percent sir.

Mr. FRANK. And any sense of how that has worked out?

Mr. FORD. Yes, sir.

Mr. FRANK. Have we had a problem with the low bidders, you know, has it been too low or what do you——

Mr. FORD. I do not know how that has worked out from the private counsel point of view, but from our point of view, it has worked out very well.

Mr. FRANK. Yes, I am only interested in our point of view.

Mr. FORD. We are averaging——

Mr. FRANK. I say that not to be callous. It is one thing, if we are talking about a government program which imposes itself on people, and then we have to decide whether it was fair or not. But where we are talking about an open competitive process, they are free to bid or not bid——

Mr. FORD. That is correct.

Mr. FRANK [continuing]. So the question then is whether this is a good deal from our standpoint and they can then make their choice as to whether or not voluntarily to participate.

Mr. FORD. In fiscal 1989, we paid an average of 28.2 percent in contingency fees on amounts collected. In fiscal 1990, so far through the first quarter, we are paying an average of 23.9 percent. I do not know how that compares with industry averages, Mr. Chairman.

Mr. FRANK. And we would assume that there has been no loss in collections overall?

Mr. FORD. No.

Mr. FRANK. I mean that is one of the things we want to find out. I would be interested to see—well, I guess it would be hard to tell, the U.S. attorney has so many other jobs, it would be hard to get a cost figure as to what it costs.

Mr. FORD. We will try to do that, because the statute requires that we do so and the GAO is going to come in and audit this——

Mr. FRANK. And see what——

Mr. FORD [continuing]. And try to compare the costs of the two.

Mr. FRANK. Well, if it is competitive bidding, obviously, some members of the bar do not like the notion of competitive bidding and there are other areas where it might be—I think it works well here—of course, we are going to have this discussion in another context with legal services—we are dealing here with a more narrowly defined task, simple debt collection, much of it, as you point out, there is no litigation involved, is that correct?

Mr. FORD. Yes, sir, contested litigation. You file suits, the debtor does not even show up and we get a default judgment and then you have to collect the judgment.

Mr. FRANK. And it is a fairly—it is not an ideological or other kinds of dispute about what to do and——

Mr. FORD. Generally not.

Mr. FRANK. Sort of hard work.

Mr. Campbell.

Mr. CAMPBELL. Thank you, Mr. Chairman.

It is a real pleasure to see you, Stu Schiffer.

Mr. SCHIFFER. It is good to see you again, Congressman.

Mr. CAMPBELL. I compliment on your work in debt collection and I am glad that I am not doing it any more.

[Laughter.]

Mr. CAMPBELL. I would like to ask you a couple of questions relative to morale. One of the factors that I recall was low morale in the U.S. attorneys offices from the debt collection burden, particularly something like the eastern district of New York, where the burden was so heavy and the work was given to the most junior person. We were talking about economics, and I will return to that, but first of all, I want to talk about psychology.

Do you share my perception that the large amount of debt collection work characterizing some U.S. attorneys offices constitutes a morale problem in the U.S. attorneys offices?

Mr. SCHIFFER. I suspect large workloads constitute a morale problem. You helped sensitize us at the Department. As I recall, you were the first official to have in your portfolio responsibility for making clear to people that dollars were important. I think part of the morale problem before that period was that people collecting money for the Government did not feel that they were doing significant work, they were not given the attention that their colleagues down the hall, who were either prosecuting criminals or defending what seemed to be sexier cases got.

What we have seen is a very healthy evolution. The U.S. attorneys have been making clear, because it has been made clear to them, that they believe that debt collection is important, salaries have been adjusted so that people doing that work are getting rewarded. I sense there are still people who occasionally are frustrated, are we ever going to get to the bottom of the pile.

Mr. CAMPBELL. I am happy to hear that. My observation was based on the fact that it was always the person with least seniority who was given the debt collection work. I wonder if that is still the case in the U.S. attorneys office.

Mr. FRANK. We were going to ask you to handle this bill in the subcommittee.

[Laughter.]

Mr. CAMPBELL. Thank you very much. I am honored. You can tell my seniority by visiting my office on the fifth floor of the oldest building.

Mr. SCHIFFER. Sometimes, Congressman, it might have been the opposite. When it was time to get rid of the Stu Schiffers of the world, the person with the most seniority was given the debt collection portfolio. In some respects, youth and vigor is really what is needed here. As Bob Ford indicated, these are not and they should not be, in the main, at least when we are talking about the small student loan cases, the large volume of small-dollar cases, they are not the stuff of which Supreme Court decisions ought to be made, and what you really need are often nonlawyers, people who are simply willing to move things along quickly and deal with volume.

Mr. CAMPBELL. That deals with the second question, is actually one I was going to get to in a bit. I am concerned about the pilot program, that it is only farmed out to lawyers. What was the thinking behind that, as opposed to going to debt collection agencies?

Mr. FORD. Well, Federal debts already, Congressman, are run through debt collection agencies. As you may recall from the process, we are the Government's collector of last resort. When a student loan, for example, goes into default, the Department of Education will try to collect it. They will then normally run it through a debt collection agency, to have them try to collect them, and only the most recalcitrant deadbeats, the ones that nobody can get to pay, are then sent to us to sue. So, when they come to us for suit, it was thought that the private counsel law firms who specialized in this business would be the appropriate people to go.

Mr. FORD. May I make one comment on the Congressman's previous question?

Mr. CAMPBELL. Before you do, if you do not mind, I just want to pursue it a second further, because you do refresh my memory. If Education, then, cannot collect the loan, will they actually sell it to the ABC Collection Agency, when ABC fails, they then give it back to Justice? I didn't think so. I thought it——

Mr. FORD. I do not think they sell it. The Education people are here. There are other programs, for example, when the agencies look at their portfolio of debts and they make an informed judgment that these debts are salable, so we will sell these, these debts we will send to the Department for litigation.

Now, before they would send them to us for litigation, I assume that they would go through the private——

Mr. FRANK. If they are here, and I do not see any reason to stand on ceremony, if there is someone from the Department who has an answer to Mr. Campbell's question, why do you not come forward and answer it. If someone from the Education Department is here, would you come forward, if you have the answer to that, rather than——

Mr. HAYNES. Mr. Chairman and members of the committee, no, we do not sell our loans. We do seek collection from the collection agency we assign it to, then we send it over to the Justice Department, they are the last resort.

Mr. FRANK. You have your hand between your mouth and the recorder.

Mr. HAYNES. I am sorry. Congressman, as I said, we do not sell our loans to collection agencies. We assign them to them and, of course, if they do not collect them, then our last resort is to send them to the Justice Department.

Mr. CAMPBELL. When you assign them to them, this is for a fee arrangement that you have or a percentage of the sum collected?

Mr. HAYNES. When I assign them where, to the Justice Department?

Mr. CAMPBELL. The collection agency.

Mr. HAYNES. Yes, we do pay them an amount for handling, if they collect the loans.

Mr. CAMPBELL. A percentage of what is collected?

Mr. HAYNES. Yes. I do not know the exact percentage.

Mr. FRANK. Going back to your competitive bid there, I would assume, is that a competitive bid?

Mr. HAYNES. Yes, the collection agencies we use are identified by competitive bidding and, on average, we pay about 29 percent.

Mr. CAMPBELL. This is very useful. I appreciate you suggesting the Education people coming forward, Mr. Chairman. It seems to me, then, that we have a system whereby the creditor makes the loan, when it defaults, deals with the collection agency on a percentage basis, if the money comes in, it is great, if it does not, it then comes back to the creditor agency who assigns it to the Justice Department for collection.

Mr. HAYNES. No, we assign it. They will give it back to us and then we send it to the Justice Department.

Mr. CAMPBELL. I used the term "collection agency" wrongly. I meant to say——

Mr. FRANK. When he said "creditor agency," he meant you as the creditor agency.

Mr. HAYNES. OK.

Mr. FRANK. He said creditor agency and you are the creditor agency.

Mr. CAMPBELL. I should have been clearer. So, at no stage in the process presently, nor in the pilot program, is there actually a sale of the debt, now that I understand it properly, if you do not mind the correction, I think I was unclear about that.

Mr. FORD. Not in his program, but, for example, I was in Agriculture the other day and I was talking with them and they do sell some loans and OMB and various agencies have sales of debts in the prelitigation stage and I assume—I do not know whether that is determined by the agency statute or the program, but there are sales of some debts and loans.

Mr. CAMPBELL. All right. Now, this pilot program that we are describing as to which we have 1 year of data deals only with farming it out to litigation on a percentage basis?

Mr. FORD. Correct.

Mr. CAMPBELL. Not collection agencies, because you assume that has previously been done?

Mr. FORD. That is one of the gripes that my private counsel have. They call these debts "second placements" and they are very upset, because they do not like "second placement" debts. They want them before the collection agencies get them.

Mr. FRANK. Let me make a suggestion. When we get to the Department of Agriculture, it strikes me that one reason there may be a difference between the Agriculture Department and the Education Department is Education has some real personal loans, whereas, in Agriculture they would be more business loans, and I assume in that market a personal loan might be harder to sell than a business loan. I would think there would be more people who want to buy to sue——

Mr. FORD. To sue.

Mr. FRANK. Exactly.

Mr. HAYNES. Mr. Chairman and members of the committee, we do sell college housing loans.

Mr. FRANK. That would make the point, then, personal education loans, but where there is some kind of a cooperate entity or a business entity, then you do sell them.

Mr. CAMPBELL. What I am driving toward is the possibility of expanding the pilot program, that you actually sell the debts more. It seems to me that you come in and out of the system a number of times, and it might be more efficient, if you are going to sell, to sell, as opposed to farming it to an agency, having them fail and then bring it back to the Department of Justice. That is the trend toward which I am going.

Two other questions. I am concerned, I think all of us are, about the potential civil rights aspects of excessively vigorous debt collection activity. This was one of the arguments raised against the prospect of farming it out to a nongovernmental party when I was at Justice.

Can you comment, Mr. Schiffer or Mr. Ford, about how you view the activities of the collection agencies? Now I am moving beyond the attorneys, hopefully the attorneys are not violating civil rights, who knock on the door in the middle of the night, the breaking of arms and limbs and so forth, this I trust has no place in our debt collection activity and I am hoping that it will not when we farm these out. Have you monitored this in any way?

Mr. SCHIFFER. Mr. Ford is in charge of this.

Mr. FORD. We have had, to my knowledge, Mr. Campbell, no complaints about the private counsel that are under contract in our program. I could not address the question with respect to the debt collection agencies. More likely, the people from the Federal agencies could, because we do not deal with the debt collection agencies.

Mr. CAMPBELL. OK.

Mr. FORD. They send it back, as you said, to the creditor agency and it comes to us and then the debt collection agency is out of the picture, they failed to collect it.

Mr. CAMPBELL. It seems to me, though, that you would not in the normal course of things get the complaints. You, after all, are the collector. The complaints, rather, would be from the people who think their civil rights have been abused, if that does exist, if that is a problem, and it would be a Justice Department concern, it seems to me, under civil rights issues. So, I would urge the oversight—and maybe this is something we can deal with in the statute, to include an element that if there is a sale of debt, that the collection agency have some oversight responsibility as to their practices.

The last question is have is the $25,000 maximum on the pilot program. I understand that we are now talking about the larger debts being sold to the law firms. I would like to know the thinking behind that. I am skeptical of that decision, for the following reason:

It seems that there is some what economics would call cherry-picking, to get a lower rate, you might get some of the bigger ones, and by removing the bigger ones, you necessarily are going to get a lower rate for the Government or, if you will, a higher percentage charge to the Government. So the question occurs to me, why did you make the $25,000 top?

Mr. FORD. Quite candidly, Congressman, it was a compromise with the U.S. attorneys, to get their full cooperation in the program. As you may recall from your days at the Department, the U.S. attorneys generally were not in favor of bringing private counsel in. When we had the legislation passed, we tried to get their cooperation and did, and one of the deals that we struck at the beginning, because at that point the U.S. attorneys were somewhat leery of enabling private lawyers, of whom they knew nothing, to come into court in the name of the United States of America and sue Bob Ford or whoever, and they were a little bit leery, so we had to work out some compromises. We decided we would not send criminal debts at the beginning of the pilot project. We decided we would not send—and we told private counsel in the bidding, it was not our intention to send to you what we would anticipate would be contested litigation. What we need from the private counsel is the collection of the judgments that are easy to get in the post-judgment posture, and they excel at that. So, these were compromises.

Now I am trying to encourage some of my friends in the Criminal Division and everywhere, let us try sending out some criminal judgments to see if we can collect those. The $25,000 limitation at any time, any U.S. attorney who has developed confidence in the private counsel working in his or her district can send out cases over $25,000 at any time they want.

Mr. CAMPBELL. Thank you. That completes my questions, but for one. I wanted to know if you—when I did the survey for the Deputy Attorney General, I remember that Baltimore was an exceptionally good debt collection program. Is that still the case?

Mr. FORD. Yes, because of Geri Zinzer.

Mr. CAMPBELL. Exactly. I was about to mention her. Well, grand. It is nice to have you gentlemen here.

Mr. FORD. Congressman, one thing I would like to add to what Mr. Schiffer said in relation to the morale problem. The administration, particularly the Treasury Department, has been very helpful. They have awards every year that recognize outstanding debt collection operations in U.S. attorneys offices and other places, and these people are brought to Washington and actually get to meet the Secretary of the Treasury and they get cash awards and that helps. It has been a big help in raising the morale and making the people think that somebody cares.

Mr. CAMPBELL. You prompt one last question. I am sorry, Mr. Chairman, you have been very patient with me. Do the candidates for U.S. attorney still get run by the debt collection czar?

Mr. FORD. No, but I wish they did.

Mr. CAMPBELL. OK. That was——

Mr. FORD. That was one of the programs that you started and we did it for a while——

Mr. CAMPBELL. One of the initiatives.

Mr. FORD [continuing]. But I think it would still be helpful.

Mr. CAMPBELL. OK. Maybe we should. Thank you.

Mr. FRANK. Mr. Campbell asked a couple of very useful lines of questions, in my judgment. One, on the complaints, I would hope you would do outreach. If we had heard a lot of complaints, I think we would have heard them and we in Congress would have gotten some complaints. If people would complain, they would have figured it was Federal and they would have complained to the Members of Congress and they would have filtered to us and we have got none, to my knowledge, and the staff confirms that. But it would still be helpful and we might do outreach to State consumer agencies in those areas, to see whether there are complaints. My guess is that we probably have not had too many or any at all and I am pleased with that.

The other, I was a little disturbed about the $25,000 limit and I had not—there is nothing in the statute that puts that limit on, right?

Mr. FORD. That is correct, sir.

Mr. FRANK. Well, the notion that Congress authorizes a program and that we did not have to bargain with the U.S. attorneys to get them to be supportive of it, so we put a limit on it that had not been anticipated is very troubling. I would hope that we could just not have that kind of attitude. That is just crazy.

Mr. Schiffer, you talk about institutional bias, I just do not have any patience for that, no understanding of it. People are very busy and we are talking about things that were not being collected, and the notion that we had to negotiate a compromise on something with some of the possible negative consequences that Mr. Campbell mentioned bothers me very much.

Mr. SCHIFFER. I confessed my bias, only to have it discounted, and then tell you what a fair person I was. I think the problem that was perceived and the problem that led to this program, as I said, was in the large-volume, small-dollar cases. I have not heard criticisms that the Department is not vigilant in going after the——

Mr. FRANK. Well, $30,000 and $40,000 these days is probably not——

Mr. SCHIFFER. I did not want to quibble over——

Mr. FRANK. I do, Mr. Schiffer, we have to quibble, and I think, frankly, you are trying to take back what you were honest enough to say, so why don't you leave it where it was. I think there is an institutional bias in the Department. I think that is a grave error. I am sorry that people have to be told that collecting money owed the Government is important. I would have hoped they would have understood it. I will be glad to participate in any ceremonies that help get that point across, given the nature of the Government's fiscal problems today, especially.

But in particular, I do not think—you know, I am sure they go after multimillion-dollar judgments, but $25,000 is pretty low today, with the kind of activity and I am very disappointed that it had to be bargained into being supportive of doing an active project.

Mr. FORD. Well, I hope I did not create the impression that they were intransigent, digging in their heels and this, that and the other, but it was a brand new program, Mr. Chairman.

Mr. FRANK. You are trying to take back and be nice to them and I just reject that. I think you told the truth the first time, that they did not like it, they were reluctant, they took it as criticism, they reacted—you know, bureaucracy has a lot of good things about it, it has some bad things about it. It sounds to me like we have the worst aspects of bureaucracy here, "You're criticizing me, you're saying I'm not doing the best possible job," and the answer was no, we are saying given the resources that we give you and what we think you do better and what other people do better, we think this is a useful way to go. I am very disappointed to hear that and I think we will have to look at that in terms of the reauthorization, we are where we are now, but it is a 1-year thing and I think we may have to address this question of a ceiling, what is your intention with regard to that ceiling, how you should be—the U.S. attorney, now what his or her option can raise it.

Mr. FORD. Conditions vary in the U.S. attorneys offices around the country. Their debt collection caseloads vary tremendously. One district, for example, may have a very heavy load of cases from the Department of Agriculture and practically none from the Education Department, and vice versa in another district. We have tried to maintain a modicum of centralized control, at the same time to have a maximum flexibility to recognize local conditions. I could not——

Mr. FRANK. I understand, but I do not understand why a $25,000 ceiling is a necessary part of that. It seems to be a fairly low ceiling.

Mr. FORD. Well, what I was trying to get to, I guess in a long-winded way, was there may well be over $25,000 cases going out to private counsel right now in some districts, where the U.S. attorney and the private counsel have worked together long enough to establish a confident working relationship.

Mr. FRANK. When a law is passed that mandates a program that seems to be a perfectly reasonable one, I do not think we should have to wait for the U.S. attorneys to reach a certain competence level for that program to be carried out without an artificial restriction, and that is something that I intend to return to, because that is what you are telling me, that when the U.S. attorney really feels comfortable enough about it, he or she says, well, we will not have that limit. If the limit does not make sense, and it does not, I am really troubled by it. I appreciate my colleague bringing it up. I am going to think some more about that and I would advise you to reconsider that. I do not really think it is in the spirit of what we did, for us to pass the pilot project.

I understand, if we are talking about $1 million, that is a different story, but $25,000 seems to be awfully low for this and may account, in part, for the relatively low collection rate we are getting.

Mr. Smith.

Mr. SMITH of Texas. I do not have any questions.

Mr. FRANK. Thank you. We will dismiss our friends from the Justice Department and we will ask Mr. Franks from the Agriculture Department to join Mr. Haynes at the table. You may proceed, gentlemen, and, without objection, we will put your statement in the record.

You may proceed. Why don't we start with you, Mr. Haynes, since we already warmed you up.

STATEMENT OF LEONARD L. HAYNES III, ASSISTANT SECRETARY FOR POSTSECONDARY EDUCATION, DEPARTMENT OF EDUCATION

Mr. HAYNES. Thank you.

Mr. Chairman and members of the subcommittee, it is a pleasure to be here and testify in support of the extension of the private counsel debt collection pilot project.

As you know, we at the Department have a comprehensive and effective debt collection process and, using the tools that are available to us, we have been able to increase our collections for each of the past 4 years from $458 million in fiscal year 1986 to $633 million in fiscal year 1989.

One of the important tools now available to us, of course, is litigation by the U.S. attorneys as a part of this process and, as I said previously, the U.S. attorneys are the collectors of last resort.

The use of private counsel by the U.S. attorneys has great potential for improving the Department of Justice's ability to enhance the debt collection process and the credit management effort, and extension of this pilot project is critical, we feel, to the data necessary to determine the effectiveness of the use of private counsel in Federal debt collection.

With your permission, Mr. Chairman and members of the subcommittee, I have prepared materials for the hearing record that briefly describe the student loan programs, the default problem and measures that we are using to collect defaulted student loans. Summarized, they are, as follows:

As of the end of fiscal year 1989, the cumulative student loan commitments were $112 billion. As of March 31, 1990, unresolved defaulted student loans held by guarantee agencies and the Department constituted $8 billion, and we estimate that gross new student default claims will be approximately $2 billion by fiscal year 1990.

The Department has increased collections on defaulted student loans over the last 4 years, as indicated: In fiscal year 1986, collections totaled $458 million, in 1987, $553 million, and in fiscal year 1988, $556 million, and in fiscal year 1989, $633 million.

For fiscal year 1989, collections on defaulted student loans came from the following sources: From guarantee agencies, $314 million, Federal collections totaled $319 million, including $187 million from IRS offsets, $121 million from Federal staff/collection agencies, and $11 million from the Department of Justice.

In terms of the collections process, the regulations that prescribe specific debt collection rules that lenders, guarantors and schools must follow to collect debts are contained in the Perkins loan and GSL program regulations, respectively. Once defaulted student loans are assigned to the Department, a detailed collection process is employed. As indicated, we do our best to collect the funds. If not, we turn it over to a collection agency and then, after a period of time, if that is not successful, then, of course, it goes to the Justice Department.

In addition, we are able to collect from Federal employees by way of garnishment moneys that are owed us by those Federal employees that are in default.

In terms of credit management and debt collection legislation, we support legislation that would extend the pilot project, because private counsel we feel has the potential to give the Department expanded use of litigation as a collection tool.

Because the Department's defaulted student loan accounts, on average, have a relatively small balance of about $2,500, we believe the use of private counsel to collect and litigate on small balance accounts, like defaulted student loans, will free scarce Justice Department resources for larger balance accounts of Federal agencies and generate more money for the U.S. Treasury.

Furthermore, Justice recently advised the Department that it would waive the requirement that Education provide Justice with the name of the debtor's employer on any litigation referral to districts participating in the pilot program. This waiver means—and this is a key point—that the Department will be able to increase by 50 percent its litigation referrals to private counsel pilot districts, without increasing our own staff resources.

For example, during the first 18 months of the pilot, with 5 districts participating in the pilot program, the Department referred approximately 2,800 cases to these districts. The Department had previously estimated that it could produce 6,000 referrals during fiscal year 1991 to the 10 pilot districts that will be participating in the program. Now, with this waiver, we will be able to produce 9,000 referrals, with an estimated value of $23 million to the ten pilot districts, if this legislation for the pilot is passed.

In other words, what we are saying to you, members of the subcommittee, we are in support of the pilot project. We feel that it will have net returns greater than what we would have had were it not for the pilot, and we are pleased to respond to any questions you may have at this time.

[The prepared statement of Mr. Haynes follows:]

Prepared Statement of Leonard L. Haynes III, Assistant Secretary for Postsecondary Education, Department of Education

Mr. Chairman and Members of the Subcommittee:

It is my pleasure to be here to testify in support of the extension of the Private Counsel Debt Collection Pilot Project.

The Department of Education (ED) is committed to responsible management of the student loan programs. At the Department, we believe we have a comprehensive and effective debt collection process. We use all of the collection tools prescribed by the Federal Claims Collection Standards and OMB Circular A-129, (on credit management) to collect defaulted student loans. Using these tools, the Department has increased its collections for each of the past four years, from $458 million in Fiscal Year 1986 to $633 million in Fiscal Year 1989. One of these tools, litigation by United States attorneys, is an integral part of that process. In the Department's process, United States attorneys are the collectors of last resort. They are critically important components in the debt collection process, in ED, and in other Federal agencies. The use of private counsel by U.S. attorneys has great potential for improving the Department of Justice's ability to enhance the Federal debt collection and credit management effort. The extension of this pilot project is critical to gather the data necessary to determine the effectiveness of private counsel in Federal debt collection.

With your permission, Mr. Chairman, I have prepared materials for the hearing record that briefly describe the student loan programs, the default problem, and measures that the

Department continues to employ to collect defaulted student loans. I will summarize the contents of these materials.

<u>Background</u>

- o As of the end of fiscal year 1989, cumulative student loan commitments were $112 billion, broken down as follows:

  - Guaranteed Student Loans (GSL) - $102 billion
  - Perkins Loans - $10 billion

- o As of March 31, 1990 unresolved defaulted student loans held by Guarantee Agencies and the Department were $8 billion, broken down as follows:

  - GSLs with State and private, non-profit guarantors: $ 7 billion
  - GSLs and Perkins loans with the Department: $ 1 billion

- o The Department estimates that gross new student loan default claims will be approximately $2 billion in FY 1990

- o The Department has increased collections on defaulted student loans over the last four years:

In FY 1986, collections totalled $458 million; in FY 1987, $553 million; in FY 1988, $556 million; and in FY 1989, $633 million.

- For fiscal year 1989, collections on defaulted student loans came from the following sources:

  Net Collections by guarantee agencies were $314 million; and Federal collections totalled $319 million, including $187 million from IRS offsets, $121 million from Federal staff/collection agencies, and $11 million from the Department of Justice.

The Collection Process

Regulations that prescribe specific debt collection (due diligence) rules that lenders, guarantors and schools must follow to collect debts are contained in the Perkins Loan and GSL program regulations, 34 CFR Parts 674 and 682, respectively. Once defaulted student loans are assigned to the Department, a detailed collection process is employed. The process, which is highly automated, has the following features:

- o Collection activities by Federal staff for the first 120 days:
  - 3-6 automated dunning letters
  - automated IRS address search
  - automated credit reporting
  - Use of the Debt Management and Collection (computer) System with the following features:
    - computer terminal access to loan records
    - computer screens with unlimited collector note pad
    - automated letter feature with over 2,000 letters and notices available
    - collector workload scheduler

- o Collection activities by collection agencies (after 120 days and up to 10 years):
  - 12 collection contracts were awarded on April 12, 1990 replacing the 6 contracts previously in effect
  - collection agencies are contractually obliged to follow minimum account resolution standards (similar to regulatory due-diligence)
  - collection agencies with the best results are rewarded with additional work
  - debtors pay collection agency fees

- Collection by Federal salary offset and Federal income tax refund offset (monthly/annually respectively) after notices are sent to debtors and they have had the opportunity for reviews and oral hearings regarding their debts.

- Collection through a specially authorized one-time Student Loan Payoff Program to permit eligible borrowers who have defaulted on their Federally guaranteed student loans to repay those loans without penalties, administrative charges, or collection fees.

Credit Management and Debt Collection Legislation:

- The Department supports legislation that would extend the Private Counsel Debt Collection Pilot Project because private counsel has the potential to give the Department expanded use of litigation as a collection tool.

- The Department's defaulted student loan accounts on average have a relatively small balance of approximately $2,500. We believe that the use of private counsel to collect and litigate on small balance accounts, like defaulted student loans, will free scarce DOJ resources for larger balance accounts of Federal agencies and generate substantial, additional revenue for the U.S. Treasury.

Furthermore, DOJ recently advised the Department that it would waive the requirement that ED provide DOJ with the name of the debtor's employer on any litigation referral to districts participating in the pilot program. This waiver means that the Department will be able to increase by 50% its litigation referrals to private counsel pilot districts without increasing its staff resources.

For example: During the first 18 months of the pilot, with five districts participating in the pilot program, the Department referred approximately 2,800 cases to these districts. The Department had previously estimated that it could produce 6,000 referrals during FY 1991 to the ten pilot districts that will be participating in the program. Now, with this waiver, the Department will produce 9,000 referrals with an estimated value of $23 million to the ten pilot districts if this essential legislation to extend the pilot program passes.

Furthermore, the Administration has proposed in its fiscal year 1991 budget request that the Higher

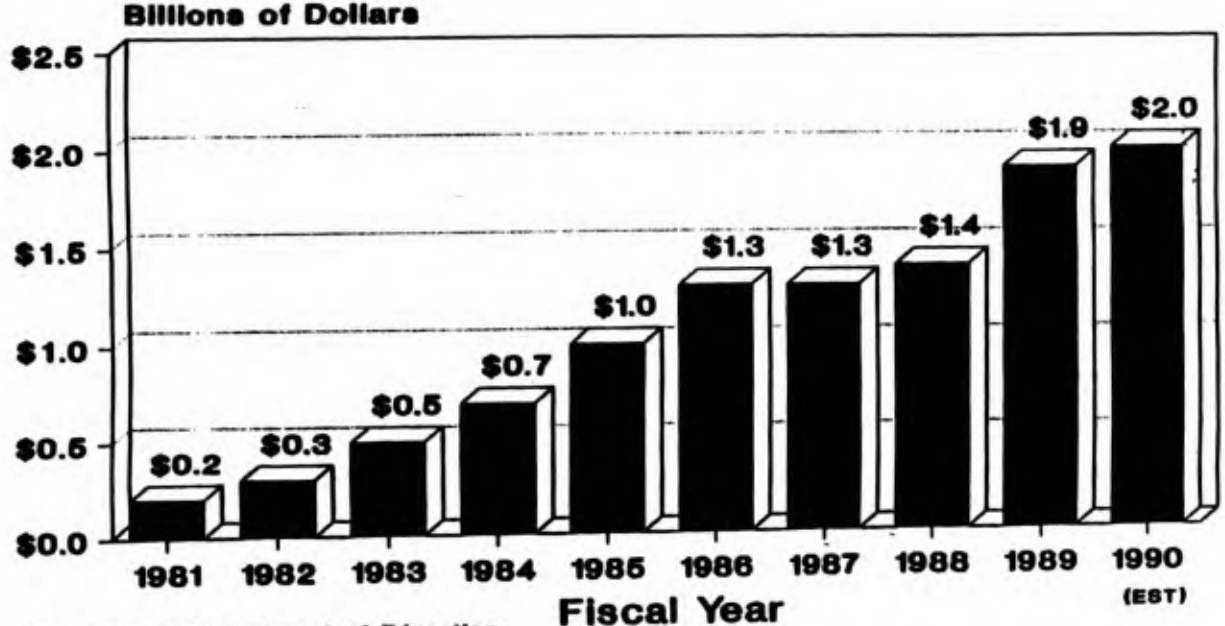
Education Act be amended to include the following Credit Management and Debt Collection provisions:

- o Credit checks for all GSL applicants who are age 21 or older and co-signers for those with negative credit histories
- o Borrowers be required to provide driver's license numbers and other skip-tracing information at the time of loan application
- o 30 day delayed disbursement on loans to first-time borrowers
- o graduated repayment schedules to be offered to student borrowers
- o wage garnishment by guarantors of student loans

Finally, the Higher Education Act is scheduled for reauthorization in FY 1992. It is Secretary Cavazos' objective to submit the Administration's Higher Education Act Reauthorization proposal to Congress in January 1991. Clearly, concerns about credit management and debt collection are paramount as we prepare that package.

I will be pleased to respond to any questions from the chairman or the members of the subcommittee.

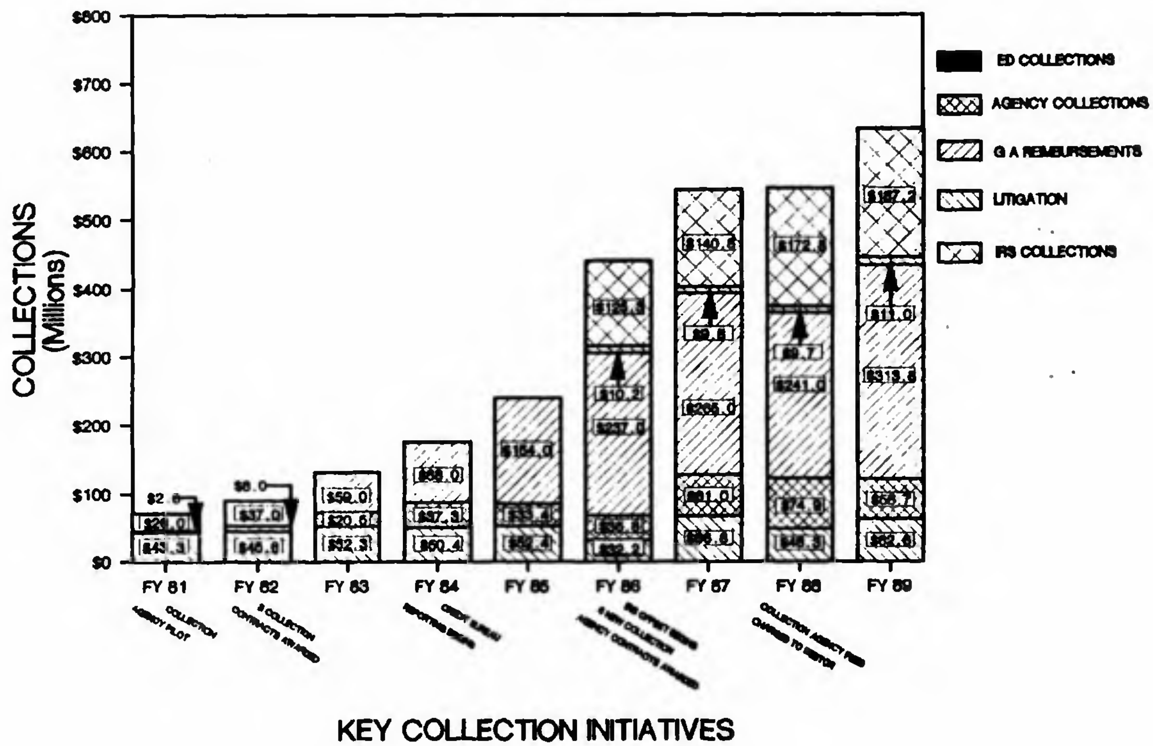
ANNUAL STUDENT LOAN
DEFAULT COSTS



Prepared by U. S. Department of Education
Office of Postsecondary Education 1990

SUMMARY OF DOLLARS COLLECTED

FY's 1981 - 1989



Mr. SMITH of Texas [presiding]. Mr. Haynes, thank you for your testimony.

Mr. Franks, will you be next?

STATEMENT OF J. ROBERT FRANKS, DEPUTY GENERAL COUNSEL, OFFICE OF GENERAL COUNSEL, DEPARTMENT OF AGRICULTURE, ACCOMPANIED BY STEPHEN BABCOCK, ASSISTANT GENERAL COUNSEL

Mr. FRANKS. Thank you, Mr. Chairman and members of the subcommittee.

I am Bob Franks. I am Deputy General Counsel for the Department of Agriculture. I am accompanied by Stephen Babcock, who is an Assistant General Counsel in our Office of the General Counsel.

We appreciate the opportunity to appear before you to set forth the views of the Department of Agriculture on H.R. 4384 and H.R. 4535.

The subject of debt collection is of great importance to the Department of Agriculture, since we have several agencies whose activities generate large amounts of receivables. Among the creditor agencies, the largest in the Department is the Farmers Home Administration. Others that are significant lenders are the Commodity Credit Corporation and the Rural Electrification Administration.

As of the end of fiscal year 1989, September 30, 1989, the Department had outstanding loans and accounts receivables of $123.2 billion. Of this amount, about $19 billion was delinquent. The majority of the Department's delinquent debt, about 76 percent, to be exact, arises from the farmer loan program operated by the Farmers Home Administration. Basically, there is about $14.4 billion in delinquent debt in that farmer loan program.

The level of delinquencies in this particular program is abnormally high because of a number of factors. These would include relaxed standards and high loan limits for emergency loans during the late 1970's, the farm crisis of the 1980's, and a court injunction that we were under that basically prohibited FmHA from foreclosing on or suing to collect any farmer program loans from about 1983 to 1988.

Now, the agency is in the process of working the large number of delinquencies through extensive debt servicing procedures that were developed under the Agricultural Credit Act of 1987. After taking these cases through these procedures, we have now begun to refer some farmer program loan cases to the U.S. attorneys for collection action, and, I might say parenthetically that obviously we have been and continue to refer other cases to the U.S. attorneys.

The Department is using as many tools as we can to collect delinquent debt. These include administrative, salary, and IRS income tax refund offsets. In some cases, such as the Rural Electrification Administration, as Mr. Schiffer mentioned earlier, the Department works closely with the Department of Justice and has workout groups that seek to resolve the delinquent loans under that program.

We also regularly send substantial numbers of cases to the U.S. attorneys offices when debts cannot be collected short of litigation. Just to give you a little bit of a reference, our own figures show that as of March 31, 1990, we had about 25,000 debt collection cases with the various U.S. attorneys offices.

We do support the pilot project to test the use of private attorneys to obtain judgments to collect debts. The statutory authorization, as I understand it, expires on September 1.

We have submitted a few debt collection cases to private attorneys in this project in the first five districts, but it is very few, largely because those first five districts are primarily urban districts and we just do not have substantial activity in those districts.

Last year, the Department of Justice did begin expansion of the pilot program into five new Federal districts. Three of those districts, specifically the district of New Jersey, the Middle District of Florida, and the Western District of Louisiana, were chosen because of the large backlog of USDA debt collection cases, primarily Farmers Home Administration cases. Of course, we are very interested in seeing how that program will work.

We do, as I say, support the extension of the pilot project. We believe that terminating the project on September 1, will not provide sufficient time to determine whether it is going to work or not work for the Department of Agriculture.

We also support the additional amendments contained in H.R. 4535. I am not going to discuss those, except to say particularly we are interested in the increase in the ceiling on the agency authority to compromise claims. We are also interested in what I would call the three interpretive clarifications to the Debt Collection Act that are contained in that legislation.

With that, Mr. Chairman, I will stop. Thank you.

Mr. FRANK [presiding]. Thank you. I have read the statement. I have no questions. I think this has been helpful to me.

[The prepared statement of Mr. Franks follows:]

PREPARED STATEMENT OF J. ROBERT FRANKS, DEPUTY GENERAL COUNSEL, OFFICE OF GENERAL COUNSEL, DEPARTMENT OF AGRICULTURE

Mr. Chairman and Members of the Subcommittee:

I appreciate the opportunity to appear before you to set forth the views of the Department of Agriculture on H.R. 4384, a bill to extend the law providing for contracts for debt collection services, and H.R. 4535, which is known as the Debt Collection Amendments Act of 1990. The Department of Agriculture supports both bills.

The subject of debt collection is of great importance to the Department of Agriculture since we have several agencies whose activities generate large amounts of receivables. The Department's largest creditor agency is the Farmers Home Administration, which is the lender of last resort providing direct and guaranteed loans for farmers, rural families in need of housing, and rural businesses and communities. Other significant lenders are the Commodity Credit Corporation, which makes farm price support loans, and the Rural Electrification Administration, which makes and guarantees electric and telephone loans.

As of September 30, 1989, the Department had outstanding accounts and loans receivable of $123.2 billion. Of this amount, $19 billion was delinquent, that is, payment had not been received by the date due. More than $14.4 billion of Farmers Home Administration's farm loans, $1.5 billion of its rural housing loans, and over $700 million of its community and business loans, were delinquent. The Commodity Credit Corporation was owed nearly $800 million in delinquent debt; the Rural Electrification Administration had over $600 million in delinquent debt; and the total of delinquent receivables owed to all other USDA agencies (such as the Food and Nutrition Service and the Forest Service) was about $1 billion.

As these figures show, the majority of the Department's delinquent debt--76 percent, to be exact--arises from the farmer loan program operated by the Farmers Home Administration (FmHA). The level of delinquencies in this particular program is abnormally high because of the coincidence of a number of factors, including relaxed standards and high loan limits for emergency loans during the late 1970s, the farm crisis of the 1980s, and a court injunction prohibiting FmHA from foreclosing on, or suing to collect, any farmer program loans from 1983 until 1988. The agency is now in the process of working the large number of delinquencies through extensive debt servicing procedures developed pursuant to the Agricultural Credit Act of 1987. Under provisions of that Act, enacted in large part as a result of the precipitous drop during the early 1980s in the value of farmland securing FmHA loans, extensive write-downs of debt are occurring on a "least cost to the Government basis". (Debts may be written down to the value of the collateral or the borrower may pay off the loan at an amount equal to what the Government would have netted from foreclosure.) After taking cases through these procedures, FmHA has begun to refer some of them to the United States Attorneys for collection action. Other claims, such as those relating to rural housing loans have been referred in the past, and continue to be referred, to the United States Attorneys for collection.

The Department is using as many tools as it can to collect delinquent debt. These include administrative, salary, and IRS income tax refund offsets. In the case of large delinquent loans made or guaranteed by the Rural Electrification Administration, the agency has established "workout" teams that, in consultation with the Department of Justice, seek to negotiate a resolution to the default.

We also regularly send substantial numbers of cases to the offices of the Department of Justice's United States Attorneys when debts cannot be collected short of litigation. These cases are typically routed from the field offices of the USDA creditor agency to the attorneys in one of the field offices of the Department's Office of the General Counsel. After a review of the case files by these field attorneys to determine that litigation is warranted, the files are routed to the office of the United States Attorney serving the area in which the debtor resides. The records kept by the General Counsel's office show that as of March 31, 1990, the Department of Agriculture had over 25,000 debt collection cases at the Department of Justice.

Because of the tremendous workload of the United States Attorneys, the Federal Debt Recovery Act, P.L. 99-578, provided for the creation of a pilot project to test the use of private attorneys to obtain judgments to collect debts. The statutory authorization for this program will expire on September 1st of this year. Both H.R. 4384 and H.R. 4535 would extend the program until September 30, 1992.

A few debt collection cases from the Department of Agriculture have been sent to private attorneys in the first five pilot districts. However, these districts are largely urban districts, and we do not have significant numbers of cases in such districts.

As is set out in the testimony of the Department of Justice's representatives at this hearing, the Department of Justice, last year, began the process of expanding the pilot project to include five new federal judicial districts. Three of these new districts--the District of New Jersey, the Middle District of Florida and the Western District of Louisiana--were specifically chosen because they have large backlogs of cases or large numbers of potential referrals of cases involving debt owed to the Department of Agriculture, most notably the Farmers Home Administration. At the present time, the contract attorneys have been selected for these districts, and we expect that cases will soon begin to be referred to these attorneys. We are waiting to see what results this program will produce.

Terminating the pilot program on September 1 of this year would not provide sufficient time to determine how well the program may or may not work for USDA, and we thus support the extension of the pilot program.

We also support the additional amendments contained in H.R. 4535 the "Debt Collection Amendments Act of 1990". I will not go into detail on these amendments, but will merely highlight several points.

This Department agrees that increasing the ceiling on agency authority to compromise claims against the Government from $20 thousand to $100 thousand makes sense. This would allow departmental agencies to resolve most small claims internally and promptly. It would also decrease the number of compromise agreements referred to the Department of Justice for approval.

We believe that the three interpretive clarifications to the Debt Collection Act that the Department of Justice has proposed in their legislation would be helpful. We are particularly interested in the amendment to ensure that the Federal Government can continue to collect interest on debts from state or local governments and can use offset procedures to collect such debts when appropriate. The issue of collecting interest has arisen in programs such as the food stamp program administered by this Department. Several appellate courts have held that the Debt Collection Act of 1982 abrogated the Government's common law right to collect interest on debts owed by state and local governments. However, a recent case (Gallegos v. Lyng, 891 F.2d 788 (10th Cir. 1989)) held that the Department of Agriculture could collect interest on a claim against a state under common law authority. The proposed amendments would eliminate this confusion.

We also support the proposal to correct the ruling by the Armed Services Board of Contract Appeals that the Government must use the offset procedures set out in the Debt Collection Act before it can offset payments due to Government contractors. The Contract Disputes Act sets up a separate set of procedures to govern disputes arising between contracting officers or their agencies and private contractors. To subject the Government to both the Contract Disputes Act procedures and to the Debt Collection Act procedures gives debtors opportunities to delay, and possibly avoid, the payment of debts actually owed to the Government.

This concludes my testimony. I thank you again for the opportunity to appear before you. If you have any questions, I will be happy to answer them.

Mr. Frank. Mr. Smith.

Mr. Smith of Texas. Mr. Chairman, is Mr. Kramer going to testify now or——

Mr. Frank. I thought he was on a separate panel—oh, he is no the same panel, I am sorry. I apologize. No, he is separate.

Mr. Smith of Texas. He is separate.

Mr. Frank. Yes.

Mr. Smith of Texas. Thank you, Mr. Chairman. I do have a couple of questions.

Mr. Frank. I did not think Mr. Kramer was at the table. I just thought maybe he would sneak up here when I was not looking. [Laughter.]

Mr. Smith of Texas. We have been told today that the U.S. Government is owed over $250 billion, and both Mr. Haynes and Mr. Franks, you all have testified that your particular departments are owed in the billions of dollars, as well.

Perhaps it was discussed before I arrived, but I think the real question is perhaps not so much how much the Government is owed, but how much could actually be collected. A lot of individuals either do not have any ability to pay, businesses go bankrupt and so forth. What is your rough estimate, based upon your own experience, as to how much of the money that is owed you is actually collectable?

Mr. Frank. Before you answer that, I am going to ask the gentleman to take over. We are going to have a Housing Subcommittee meeting, which is marking up and is supposed to be finished, and I have to exempt myself for about 15 minutes. I will be back, so you will be in the charge, the gentleman from Florida.

Mr. Smith of Texas [presiding]. We will try not to bring up too many other subjects while you are gone.

[Laughter.]

Mr. Franks. Mr. Smith, quite frankly, I do not think I can really give an estimate of how much is collectable. There are a lot of factors involved and it depends on the nature of the debt.

For example, we have fairly large REA borrowers, some of whom are in financial difficulty. Again, as Mr. Schiffer pointed out, we have workout groups working on those. Normally, a fairly large amount of that debt is paid back. There are other programs, for example the old economic emergency loan program and the emergency loan program, where the debt is fairly old and the chances of collecting much of that are probably fairly slim.

Mr. Smith of Texas. OK. What percentage of the total amount owed do those programs represent?

Mr. Franks. Of the delinquent amount, I would think slightly less than half is under those emergency loan programs.

Mr. Smith of Texas. Less than half, about half?

Mr. Franks. Less than half.

Mr. Babcock. Less than half of $19 billion.

Mr. Franks. Yes.

Mr. Smith of Texas. OK.

Mr. Haynes, what about your experience?

Mr. Haynes. Congressman, the Department of Education, of the amount owed us, we collect, on average, about 50 percent of what is owed. We are owed $2 billion, we expect to collect about——

Mr. SMITH of Texas. About half of that?

Mr. HAYNES. Yes, sir.

Mr. SMITH of Texas. You figure about half is collectable?

Mr. HAYNES. Yes.

Mr. SMITH of Texas. OK. The next question is what is your personal experience with the pilot program. I know, for example, Mr. Franks, you said you did not have much experience with it in the locations where it was in place.

Mr. Haynes, what about your experience?

Mr. HAYNES. Congressman, in terms of our own experience, we have been able to increase collections as indicated. For example, because of the pilot, we noted that in fiscal year 1988, we referred 6,300 cases to Justice and netted $24 million, and in 1989, when the pilot kicked in, we went up to 8,000 accounts and netted all total $30 million. Of that amount, $11 million came as a result of being in the pilot.

Mr. SMITH of Texas. Would you favor expanding the program? The chairman was saying earlier that he would like to increase the amount, the limit to $25,000. Would you agree with that?

Mr. HAYNES. I think that——

Mr. SMITH of Texas. Or are you doing a good enough job, where you think they should be entrusted with greater responsibility and greater debt collecting ability?

Mr. HAYNES. Congressman, let me answer this way: I think we need to get more data to properly evaluate the pilot, so I think that is why I think we need to extend it. We have no problems with where we presently are. The amounts that we normally refer are, on average, about $2,500, primarily from student loans.

Mr. SMITH of Texas. I saw the average is about $3,000, so it is well below the $25,000 threshold.

Mr. HAYNES. Yes, sir.

Mr. SMITH of Texas. Mr. Franks, what about you, would that increase the activity in those particular areas, if the amount were raised,or not necessarily?

Mr. FRANKS. Mr. Smith, I am not sure that that ceiling is particularly relevant to the Department of Agriculture. In the three new pilot districts, three of the second five pilot districts, I believe the activity is primarily going to be in the area of rural housing foreclosures, rather than in collecting debt such as post-judgment debts.

Mr. SMITH of Texas. Thank you.

I am going to yield to my colleague from California, Mr. Campbell.

Mr. CAMPBELL. Thank you, Mr. Chairman.

Mr. SMITH of Texas. Say that again.

[Laughter.]

Mr. CAMPBELL. Thank you, Mr. Chairman.

I would like to welcome you and appreciate your testimony and compliment you. This is a very difficult, but important task. Now, as you might have picked up from the previous testimony, I used to do this work at the Department of Justice before I became a professor and then to Congress, but I still need instruction and I wondered if you would help me on this.

The way the system works, as I understand it, you gentlemen, Mr. Haynes and Mr. Franks, make the first judgment as to whether a debt should be sold to a collection—that is the wrong phrase—farmed out to a collection agency, that is the first call, or whether you should use your internal processes to try to collect it. After it has failed to be collected either route, you then make a decision whether to send it to the Justice Department, and then Justice makes a decision under this pilot program of whether they will contract with the private attorney. The first question, do I have it more or less right?

Mr. HAYNES. Yes, you do.

Mr. CAMPBELL. Thank you. Then at that first judgment, as to whether you farm it out or not, you are making a judgment as to whether your resources are best used in collecting this particular debt or not. I have a very strong preconception, informed by my experience as a debt collector, that you ought to send them all out. That is to say that Government employees have other activities for which you are trained, directed, that debt collectors provide a service that is specialized, and that the bias, if there is any, ought to be in favor of farming them all out. Could you tell me why you decide to keep some of those collections in-house?

Mr. HAYNES. We have a process which we try to collect what is owed us, we allow 120 days. At the end of the 120 days, then we turn it over to a collection agency that we have contracted with.

Mr. CAMPBELL. So, it is automatic?

Mr. HAYNES. Yes, sir.

Mr. CAMPBELL. All right. That answers my question. In a sense, then, you do what I would suggest.

Mr. HAYNES. Yes, sir.

Mr. CAMPBELL. And is the same true with the Department of Agriculture?

Mr. FRANKS. No, Mr. Campbell, and let me elaborate a little bit on that. The first point I would make is that, generally, we do not use collection agencies to collect our debt. Now, that again is for several reasons. Obviously, if you have got debt from an REA co-op of several million dollars, you do not turn that over to a collection agency.

Another factor is that most of the debt that is owed to the Commodity Credit Corporation that arises out of the domestic farm programs is collected by administrative offset. In other words, the debtors are people who continue to participate in farm programs and who are eligible to receive payments in subsequent years. If they owe us debt, we offset that against the payments we would make in subsequent years, and we collect, at least in that particular program, much of the debt through administrative offset.

In the case of the Farmers Home Administration, we are prohibited by provision in our Appropriations Act from using funds to employ or contact with debt collection agencies to collect the debt, so we do not use them in that situation, either.

Mr. CAMPBELL. That is in your authorizing legislation?

Mr. FRANKS. No, that is, I believe, in the regular Appropriations Act.

Mr. CAMPBELL. It is a problem in the appropriation and it is——

Mr. FRANKS. It has been a provision in the Appropriations Act for several years.

Mr. CAMPBELL. And it says that you may not use a debt collection agency for debts above a certain amount?

Mr. FRANKS. No, it is a flat prohibition on the use of funds of the Farmers Home Administration to either employ or contract with debt collection agencies.

Mr. CAMPBELL. And can you give me any explanation of why that came about?

Mr. FRANKS. Let me point out one other thing. There is one specific exception they have had. They have had a couple of pilot projects, I believe, that they have been running that were authorized in that act.

Mr. CAMPBELL. And can you enlighten me as to why this appropriations rider was adopted?

Mr. FRANKS. Well, the committee apparently did not want——

Mr. CAMPBELL. Because Congress wanted it that way?

Mr. FRANKS [continuing]. To submit debts to collection agencies.

Mr. CAMPBELL. I believe that is a bit cycular. I wondered if there was a bad experience. Do you want to speak to that question?

Mr. FRANKS. Yes, let Mr. Babcock——

Mr. BABCOCK. I am the head of the Division of the Office of the General Counsel that handles Farmers Home Administration's legal work. We have two basic kinds of debts, housing debts and farm debts. With respect to the single-family housing program, it usually is not necessary to use a collection agency, because with the generally rising price of housing in the United States, if we can foreclose on our security, we are made whole and that is what we will be doing with the pilot program that the Justice Department is operating. That program's main utility for Farmers Home Administration will be to foreclose on single-family houses where the borrower has stopped paying, and usually the borrower has left. So, it is not a situation where we would logically employ a debt collection agency.

With respect to the farm loans, Congress has established an extremely detailed and complex set of loan servicing provisions, and we go through an extremely complicated set of calculations to determine how much they can pay and we write off the rest. Again, there is usually no situation in which it would be logical to use debt collection agencies in any mass way. We do have security in some cases.

Mr. Franks mentioned the old emergency loans and economic emergency loans. The security may not be much good and as we progress through the debt processing procedures set out in the Ag Credit Act of 1987 and get to the end of those procedures, maybe at that point we will want to use debt collection agencies. But that is a year or two or three into the future, because the borrowers have rights to administrative appeals, they have rights to mediation. If these do not work, they often file chapter 12 bankruptcy, and so it is not a situation where, even absent the statutory prohibition, we would be likely to use debt collection agencies on a large scale or on a nationwide basis.

Mr. CAMPBELL. Thank you, Mr. Babcock. I truly am not convinced, however, that you need a statutory prohibition. You have given me a very wise recitation of discretionary factors which should be left, it seems to me, with the Department. Why a statutory prohibition?

Mr. BABCOCK. The agency——

Mr. CAMPBELL. If you cannot defend it, that is fine, it may not be defensible.

Mr. BABCOCK. The agency was attacked in court, both in the housing program and in the farmer program, for being too vigorous in its debt collection activities. It has put to bed and dealt with the accusations in both court cases. Both of these were extremely lengthy proceedings, lasting years, and perhaps this congressional prohibition came out of that era. I cannot say, I was not representing the agency at the time this language first began appearing in our Appropriations Act.

Mr. CAMPBELL. Rather than extend this unduly, let me ask if you would be so kind, hearing no objection from my colleagues, if you could supplement the record with a letter, if you would be so kind. I make that request to Mr. Franks, as well as to Mr. Babcock, to just tell me of that episode, if you would, because the instance that you believe, the case that led to the statutory prohibition, I would be very benefited from knowing about that.

Mr. BABCOCK. On the farm program side, it is mentioned in Mr. Franks' testimony, *Coleman* v. *Lyng,* there was a prohibition, an injunction which was in effect for most of the time between 1983 and 1988 which prohibited the agency from taking any form of collection action with respect to farm loans.

With respect to housing loans, the case is called *Gabriel Johnson* v. *United States;* it was a class action in Alabama, which has been to the circuit court of appeals once and is still pending in the district court. I mean if you want to know more, I will be happy to——

Mr. CAMPBELL. You have given me the case names.

Mr. BABCOCK. There are pages of decisions, but I think it was the——

Mr. CAMPBELL. Mr. Babcock, what I needed was the case names and you have given that.

Mr. BABCOCK. Yes, sir.

Mr. CAMPBELL. If you would be so kind as to supplement the record with the citation, I then have all I need.

Mr. BABCOCK. Yes, sir.

[The information follows:]

United States Department of Agriculture

Office of the General Counsel

Washington, D.C. 20250-1400

MAY 14 1990

The Honorable Tom Campbell
House of Representatives
Washington, D. C. 20515

Dear Mr. Campbell:

During my testimony on May 10 before the Subcommittee on Administrative Law and Governmental Relations on H.R. 4535 and H.R. 4384, you asked for the citations to the two cases involving Farmers Home Administration's debt collection procedures that were mentioned by Stephen Babcock. The case involving farm loans is Coleman v. Lyng, 864 F.2d 604 (8th Cir. 1988), cert. denied, 110 S. Ct. 364 (1989). The housing loan case is called Gabriel Johnson, et al., v. U. S. Department of Agriculture, 734 F.2d 777 (11th Cir. 1984). Proceedings to implement the court's decision in Gabriel Johnson are still pending in the Federal District Court for the Southern District of Alabama, Civ. No. 80-0836-BH.

I am also enclosing an excerpt from Senate Report 99-438, to accompany the agriculture appropriations bill for fiscal year 1987. This explains the provision prohibiting the Farmers Home Administration from using private debt collection agencies. You had asked for background on this provision. The current provision is section 631 of P.L. 101-161.

If you desire further information, please let me know.

Sincerely,

J. Robert Franks

J. Robert Franks
Deputy General Counsel

Enclosure

cc: The Honorable Barney Frank
Chairman
Subcommittee on Administrative Law
and Governmental Relations
House Judiciary Committee

The Honorable Craig T. James
Ranking Minority Member
Subcommittee on Administrative Law
and Governmental Relations
House Judiciary Committee

place additional emphasis on identifying borrowers eligible for graduation and initiating action to remove them from the FmHA portfolio.

RDIF ASSET SALES

The Omnibus Reconciliation Act of 1986, as reported by the Senate Budget Committee (S. Rept. 99–348), includes a provision to allow sales of the assets of the Rural Development Insurance Fund [RDIF]. Such sales would necessarily remove Farmers Home from all requirements to service those loans. This servicing has included subsequent loans and/or grants when necessary. Farmers Home has done an excellent job in servicing these loans because of its understanding of the needs of rural communities. The Committee is deeply concerned that private lenders may not afford similar considerations. Therefore, the Committee directs that no sale of assets be made to a purchaser who cannot certify that it has the ability and intention to service such loans in a responsible manner.

PRIVATE COLLECTION AGENCIES

The Committee has included bill language prohibiting the Farmers Home Administration from making use of private debt collection agencies to collect delinquent payments from Farmers Home Administration borrowers. The Committee feels that the use of such agencies may restrict the rights of borrowers, and renders FmHA incapable of making use of a wide array of alternatives already available for resolving debt collection and borrowers' credit problems. Because of the current state of the farm economy, FmHA should be sympathetic to the farmers' problems and should use local FmHA personnel for servicing the loans, including debt collection.

RURAL ELECTRIFICATION ADMINISTRATION

The Rural Electrification Administration [REA] was established by Executive Order 7037 on May 11, 1935, to provide loan funds to eligible borrowers for the purpose of extending central station electric service to unserved persons in rural areas. Statutory provision for the agency was made in the Rural Electrification Act of May 20, 1936. On July 1, 1939, under Reorganization Plan II, REA became a part of the Department of Agriculture. On October 28, 1949, the purpose of REA was expanded by Public Law 423 which amended the Act to authorize loans for furnishing telephone service to rural areas.

Public Law 93–32, enacted May 11, 1973, amended the Rural Electrification Act of 1936, as amended, by establishing a Rural Electrification and Telephone Revolving Fund [RETRF] for the purpose of making insured loans to REA electric and telephone borrowers. Loans made under this authority bear either 2- or 5-percent interest in accordance with criteria specified in the act, and have a maturity not to exceed 35 years. The act also authorized REA to guarantee loans made by other lenders at rates and terms agreed upon between the lender and the bor-

Mr. CAMPBELL. I have one last question to Mr. Franks and to Mr. Haynes. The $20,000 maximum presently, as to your ability to compromise, is the subject of some of the legislation we are reviewing today, whether we should go beyond that $20,000, and I understood Mr. Franks to be supportive of going above the $20,000 limit as to how much you can compromise. First of all, let me ask you, if I have your statement correct, Mr. Franks and then if Mr. Haynes could tell me, if you also believe you should have higher authority.

Mr. FRANKS. Yes, Mr. Campbell, we do support going above the $20,000 limit, to allow the agencies to settle above that amount.

Mr. CAMPBELL. And would you have a maximum in mind?

Mr. FRANKS. We support the bill, H.R. 4535, and that goes to $100,000.

Mr. CAMPBELL. Thank you.

Mr. Haynes.

Mr. HAYNES. Congressman, we have no problem with a higher amount.

Mr. CAMPBELL. But affirmatively, do you seek a higher amount? Do you think that the Department of Education is appropriately using its discretion in settling these cases in a way that is preferable to having Justice do it, so that you should have the right to go ahead and settle above $20,000? That is what is called a leading question. The answer is yes?

Mr. HAYNES. Yes.

Mr. CAMPBELL. Thank you.

Thank you very much, Mr. Chairman.

Mr. SMITH of Texas. Thank you all for your testimony. We appreciate your coming here today.

We have one more witness before us and that is Mr. Kramer, if you would come forward.

Our next witness is Donald Kramer, of St. Louis, MO. Mr. Kramer, let me say to you that I am going to need to yield the chairmanship, and that is a nice phrase I like to use, to my colleague, Mr. Douglas, and he will continue with this hearing.

STATEMENT OF DONALD B. KRAMER, ESQ., KRAMER & FRANK, P.C., ST. LOUIS, MO

Mr. KRAMER. I hope you will have an opportunity to ready my testimony. It is somewhat controversial.

Mr. SMITH of Texas. I am scared of leaving now.

[Laughter.]

Mr. KRAMER. I can do it in 4 minutes.

Mr. SMITH of Texas. That is a deal.

Mr. DOUGLAS. He would be nervous about leaving you and me to work things out.

[Laughter.]

Mr. KRAMER. You are talking to someone down in the trenches and I do not benefit from the pilot project, I am not in a pilot district. I am an attorney whose life is collections. I have been in it since 1954. I have a staff of 101 people and I serve many banks and credit unions and national corporations. I have offices in four States.

I support the pilot project, but I submit that this has not been a pilot project. If you will look at my materials that I have submitted to you, you will see that all the attorneys that have been involved in this have been getting junk. They have been getting what we call second placements, they have been worked by agencies, they have been worked by the U.S. attorneys office, and so when you see a small return on the figures that the chairman was referring to earlier, it is because it is a miracle they are collecting anything, because of the age and the previous handling.

There were comments about why are we not getting claims over $25,000. Actually, the most collectable unsecured claims are in the $5,000 area. The $3,000 to $6,000 claims are the most collectable areas from the retail consumer. When you get a claim over $25,000, that person is very liable to go into bankruptcy.

Also, in connection with previous testimony, when you talk about agencies, remember, they cannot sue, all they can do is make a phone call, make pressures other than suit. Those attorneys who are in the pilot project can sue.

I urge you to look and see what is happening to claims under $500. I do not mention it in here, because it might be embarrassing to people. Remember that collection law is mainly techniques, rather than actual trial room work. That is why the U.S. attorneys office is not anxious for this work.

But the biggest thing today is where are these accounts, where are the billions, where are the millions? We are hearing figures of the placements here, and if you will look at those figures, it is remarkably small and, as I say, it has been junk. I urge you to look and see what has happened to all of those claims.

You have heard about a moratorium on foreclosures from 1983 to 1988. When I heard a figure of 100,000 foreclosures that have never been handled—and that is mentioned in here—I wonder what happened to them, in what drawer they are sitting.

I think the U.S. attorneys office ought to be doing other things other than collections and I think they understand that, too. They can handle the bigger items, the trial items. We in the private sector believe we can do a wonderful job for you, if the work is placed promptly. But if you look at what happens in the private sector, in retail claims, and that is claims against consumers, you are talking about items that have to be placed at about the 120-day level. And I was pleased to hear the Education Department was thinking about that particular figure. We have got to have claims promptly, because the level of collection drops dramatically, once you go beyond that level.

I want also, while I have your ear, to caution you that chapter 13 bankruptcies are now being used to wipe out student loans. In St. Louis, the typical bankruptcy, the chapter 13, the typical plan calls for 30 percent for student loans, Government insured student loans, and the judges are granting it all over the country, because they feel they have to, the way the law is set up. You are going to get wiped out on 70 percent of your student loans. I would think that any attorney who files a chapter 7 bankruptcy for a person with a student loan might be guilty of malpractice, because they do not take advantage of the chapter 13 the way it is today.

I only represent creditors. I do not represent debtors. I suggest that you give the private sector the ability to collect these accounts for you, make it a truly pilot program.

Let me just take a glance at my other notes here. I do not urge you to sell these accounts. I think what you will get for them is next to nothing. In the first place, the age of them means that you will probably get 3 to 5 cents on the dollar, if you are lucky, and I do not know whether there is that much money out there in the purchasing community to really buy all these claims. You can collect a much greater percentage if you place it with private counsel.

I want to comment also that Bob Ford of the Justice Department has been very cooperative with the private sector. He has been extremely willing to assist us. When they ask for bids on this project, 1,177 offices asked for bidding. Only 85 bid on it, because of the problems that they saw in it. When they asked in the second five pilot districts, 431 asked for bidding information, and only 31 bid on it. It is because the private sector does not see the good claims coming. They can do a wonderful job for you, if you just give them an opportunity to do it, but agencies are not necessarily the answer, unless you can give them the authority to pass these on to attorneys.

The process described by Congressman Campbell here, where it goes from one to another to another to another, it ends up with the attorneys years down the line and I think you may find that $6 million a day is going beyond the statute of limitations, because of the delays. You have got a wonderful chance to collect, if you use the pilot project.

Thank you.

Mr. SMITH of Texas. Mr. Kramer, thank you for your testimony. You were true to your word, but you were candid as well as controversial, and that is much appreciated.

Also, I think you have had a number of good suggestions that we ought to consider.

[The prepared statement of Mr. Kramer follows:]

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REPLY TO ST. LOUIS,
MISSOURI OFFICE

SUMMARY

TESTIMONY OF DONALD B. KRAMER, ST. LOUIS ATTORNEY
COMMITTEE ON THE JUDICIARY
SUBCOMMITTEE ON ADMINISTRATIVE LAW & GOVERNMENTAL RELATIONS
MAY 10, 1990

"Pilot" Project is not a "Pilot"

(a) Not enough claims placed.
(b) Only "junk".
(c) Districts are not representative.

Where are the claims?

(a) Only $7 billion pending, out of a total of more than $32 billion.

(b) Claims going beyond Statute of Limitations ($6 million per day?).

(c) What happened to 100,000 foreclosures?

(d) Speed up processing.

Attorneys hampered by "red tape"

(a) Allow negotiations, permitting some discretion for small reductions.

(b) Allow discretion in use of letters and pleadings.

Improve laws to assist recovery

(a) Stop Student Loan losses in Chapter 13 cases.
(b) Allow garnishments in all states.
(c) Permit assistance in tracing by government agencies.

PROPOSED TESTIMONY OF DONALD B. KRAMER

May 10, 1990 - 10:00 A.M.
House of Representatives
Committee On The Judiciary
Subcommittee On Administrative Law & Governmental Relations

Mr. Chairman, Members of the Committee, and members of the public My name is Donald B.Kramer. I am an attorney from St. Louis, Missouri, speaking for myself and not for any organization, appearing at your invitation, but at no expense to the government. I am not in a "pilot" district. My awareness of the "pilot program" comes from having been Chairman for two years of a committee of the Commercial Law League of America, designated to develop information on the Federal Debt Collection project. I currently serve as Advisor for that committee. I have met on several occasions with the Deputy Assistant United States Attorney in charge of the project for the Justice Department. My professional awareness comes from being President of Kramer & Frank, P.C., a law firm devoted exclusively to the collection of delinquent accounts for creditors, including in my clientele eight major bankholding companies, 80 credit unions and many major national corporations; with a staff of 101 people in four offices located in Missouri, Illinois and Kansas.

I appear here in support of a "pilot" project to allow private attorneys to assist in the collection of non-tax Federal debt. There was passage of the "Federal Debt Recovery Act of 1986" (Public Law 99-578), but a <u>real</u> "pilot" project has not existed. Almost three years were spent developing a bidding process, developing a computer system, and in fiscal 1989 placing 3,647 mainly "junk claims" totalling $14,266,391 in just five "pilot" areas. In the fiscal year 1990 through March 7, 1990, the Central Intake Facility only placed 617 claims with private counsel, totalling $3,776,207. Commercial claims under $25,000 were not being sent at all. What happened to the 10,452 cases totalling $131,100,000 the U.S. Attorney said were ready for transmittal in April, 1987? The "pilot" project did not become "operational" until September, 1989. The first five districts originally selected represented districts where the U.S. Attorney was having the most trouble in collecting accounts. That is not a "pilot". Items placed for collection were "junk", consisting mainly of "second placements", items that had previously been worked by the U.S. Attorney or by collection agencies. In most cases the claims were in the form of judgments that the U.S. Attorney was unable to collect. Attorneys were advised they would not be receiving fresh claims. Many prime collection law firms refused to bid because they didn't want to complete an 111-page form, revise their whole computer system, and send two people to a one-week course, just to receive "junk". Most of the firms bidding realized they would lose money, but hoped that later claims received would not be "second placements".

colleotion law ie mainly teohniques rether than the actual court room trial work. Attorneys in the Justice Department probably have little desire to be burdened with the administration of oolleotion aocounts. The government needs the techniques and skills developed by the private sector, whioh have an incentive when standard contingent fees are permitted.

But where are the eccounte? In eerly 1986, the Office of Management end Budget reported that nearly $20 billion in non-tax delinquent dsbte was owed to the U.S. Of that amount, more than $6 billion was more than eix yeare old! By September 18, 1989, the O.B.M. wee eetimating the non-tax delinquent debt at $32 billion. Where are theee aooounts and why aren't they being plaoed promptly for collection? Three yeare ago at a Washington hearing, I heard a etatement that every day six million dollars' worth of these non-tax claims were going beyond the etatute of limitations. It'e not hard to believe if you saw a report in The Washington Post on February 21, 1990, indicating the IRS loses $2 billion to $3 billion each yeer because of the expiration of a eix-year statute of limitatione. If there is $32 billion in non-tax Federal delinquenoies, the U.S. Attorney cannot handle it all! Richard Thornburgh, Attorney General of the United Statee, eeid in January, 1990, there were 84,000 civil and oriminal cases currently pending to colleot $7 billion. During the course of my inveetigation, it was mentioned that there were 100,000 foreclosures that were not being proceeeed, mainly for political reasons, since no Senetor or Representative wanted to devote court coste to oonduoting forecloeures in their state or dietrict, particularly when farmere were involved. But why can't we et leeet file suit on the notes, or work out tiny pey programs? Just $100.00 psr month from 100,000 debtors would mean millions. At preeent, ell payment arrangemente must be in writing and approved by the government, through the local U.S. Attorney. The approval processe is time-consuming. No prinoipal, interest or court costs mey be waived. I suggest that billions of dollare in claims may very well be in the filee of your Federal agenoies, hidden from view, since no one has the time to devote to prooeseing theee claims and eince many of the Federal agenoiee feel thet if they turn it over to the U.S. Attorney, little time will be available for handling. While the U.S. Attorney'e office hae a very intelligent staff, and the direotor of the program is trying desperately to do a good job, they are mired down in volume end "red tape."

On August 30, 1989 the Department of Education announoed they "would seek to collect 100,000 defaulted Federally guaranteed student loans that etate agenoiee have been unable to recover". The 100,000 loans involved about $300 million, offioials said. Did these olaims get plaoed promptly? The default rate et 1,040 eohoole at over 30 percent in 1987 wae obsoene. If private industry allowed such rates, most major firms would be bankrupt overnight! Defeult costs are expected to soer to $2 billion in 1990 in the etudent loan area. Because the retail attorney industry ie not organized, there is no perticuler group pounding on your door, euggesting that e wonderful job could be dons if claims were just placed promptly. If they were allowed to file lawsuits, not forced to cheok with the U.S. Attorney bsfors making a movs, not forced to use "generic" letters and pleadinge prepared by the U.S. Attorney, and permitted to make it worthwhile for a debtor to etert making payments rather than force litigation (by being ellowed to negotiate down to the principal amount and, perhaps, waive eome of the interest or penaltiee in return for a pay program or a prompt reduction of the claim) -- then we could make eome real progrees.

I caution you that the Chapter 13 Bankruptcy ie now being used by some attorneys ae e device to circumvent the law which would have prsvented the diecharge of etudsnt loans that matured within five years of the filing of the petition. Cen't Congress provide us with a law to prsvent the discharge of Federal loans through the Chepter 13 Bankruptoy as they did with Chapter 7 casee? Section 222 of the Staford Student Loan Default Prevention and Management Act of 1989 providse for the establishment of a three-year study on the discharge of student loan indebtedneee in bankruptcy proceedinge. I believe creditors' attorneys can tell you the results right now -- that consumsr attorneys will take advantage of every loophole they find. When they found so many ways to hurt creditore in Chapter 13, filings went up 70 psrcent since 1985.

Coneider meking the lawe uniform in the United States releting to the gerniehment of e paycheck to ellow the Federal Governmsnt to get ten percent of the dieposable income of a dsbtor in all statss, with gernishments that might run 90 days at a time. I rsmind you thet severel etatee do not have normal garnishment laws, and this pute the collecting attorney at a eevere dieadvantage. And, should Federal employses remain exempt from wage garnishment for debte owed to the governmsnt? Paes HR895 "Fair Garnishmsnt Practicee Act of 1989".

Will you allow the facilities of the Unitsd States to be available for the tracing of debtors? Perhaps even ueing ths facilitiee of the Sooiel Security Administration or Internal Revenue Service (although I realize that may be prevented by rules and regulations). I certainly would not want the legislation to be bogged down for years while considsring such a thought.

Speed up the procese of placing claims from the Federal agency to attorneye. Currently you ars paying dearly for a "central intake facility", which is receiving $140.00 per fils for the procsesing of eaoh oleim. If you incrsass the number of claims, psrhaps it warrante a contingent fee, as is now charged in the private sector when collection agencies proceee claime to private attornsys. Perhepe you must require at lsast 25 percent of ths non-tax undieputed claims, whioh have not made paymsnt in the leet 120 days, be pleced by Fedsral agencies immediately with the privats seotor. If you will examine the records of the oredit oard industry to eee how the ege of en account relates to the collectability, you would be plecing mattere at the 120-day level.

I suggest that you conform to collection industry standards by allowing the ettorneye to colleot the funds in their own offices and have them remit the funde to the Federal Government after deduoting the authorized fee, rether then current procedures of transmitting checks to the Treesury, weiting for payment of fee, and delaye. Use bonded attorneye to evoid improper withholding of funds.

Summarizing:

1. Make this truly a "pilot" project.

2. Pleoe claims promptly and not make them "second plecements".

3. Allow the ettornsye in the collection industry to use the skills they have developed through the years.

When I entered the praotioe of lew in 1954 in the collection industry, I began handling oolleotions and bankruptcy items for creditors. Both of theee ereas were not feehionable, and the large "silk stocking" firms did not want to touch e oollection or a bankruptcy matter. That situation hes changed dramatically in the last few years, and there is hardly a major law firm in this country today that does not have a benkruptcy departmsnt, sinoe they find there are some greet fees to be earned in the bankruptcy ersa.

If the private seotor would be permitted to really collect delinquent aocounts for the Federal Government promptly, they would develop more efficisnt methods to make eubstantial fses on e contingent basis, and you would see major firms entering ths arena. The private sector, if given e fair chance, could do wondsrs for you!

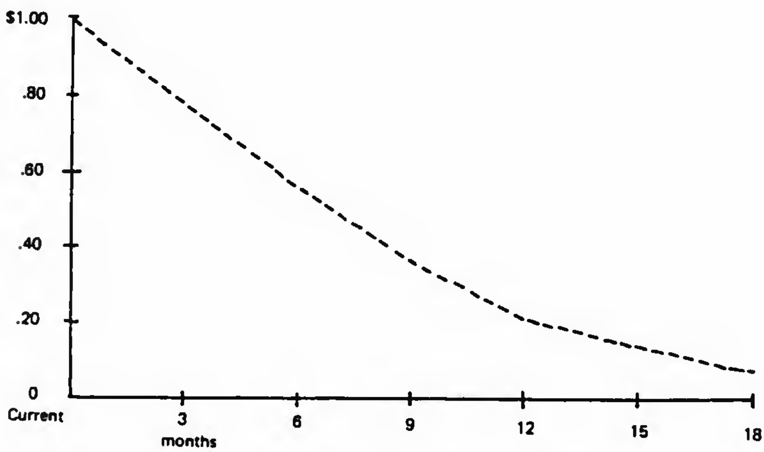
The Key to collecting the eeriously dslinquent account is the lawsuit--not just letters or phone calls. Don't loss sight of what Senator D'Amoto said in October, 1986, "This legisletion makes available to the Governmsnt the eervicee of attornsys who have demonstrated competency, experience and reliability in the handling of collection accounts."

VALUE OF PAST DUE ACCOUNTS

Every credit grantor knows that the longer he waits before attempting to collect, the less likely it is that the debt will be paid. The reasons include these factors:

1. Job loss.
2. Marital problems.
3. Skips.
4. Illness.
5. Other creditors acting faster.
6. Bankruptcy.
7. Accidents.

Yet, some credit grantors still send out three or four or even more statements and letters before starting more direct and aggressive collection efforts. While they are doing this, their accounts rapidly become increasingly uncollectable, and drop in value just as fast as the line on the chart.



Estimated rate at which uncollected past due accounts lose their value.

SOURCE: AMERICAN COLLECTORS ASSOCIATION, INC.

SOURCE: DEPARTMENT OF JUSTICE

DEPARTMENT OF JUSTICE

CENTRAL INTAKE FACILITY

FY 90 STATISTICS thru 3/06/90

U.S. ATTORNEY'S OFFICES

	DEBTS	REFERRED VALUE	$ COLLECTED	$ NOT COLLECTED
NEW DEBTS	543	$ 22,058,245		
CASES CLOSED	185			$ 5,061,363
NET COLLECTIONS			$ 6,364,398	

Pending at
3/06/90: 5,254 cases with current balance of $114,800,495.

PRIVATE COUNSEL FIRMS

	DEBTS	REFERRED VALUE	$ COLLECTED	$ NOT COLLECTED
NEW DEBTS	617	$ 3,667,207		
CASES CLOSED	30			$ 110,633
NET COLLECTIONS			$ 495,926	

Pending at
3/06/90: 4,350 cases with current balance of $21,374,023.

Private counsel contingency fees in FY 90 = $ 104,417 (21.08%).

Disbursements paid private counsel in FY90 = $ 8,606.

USAO/PC COMBINED

	DEBTS	REFERRED VALUE	$ COLLECTED	$ NOT COLLECTED
NEW DEBTS	1,160	$ 25,725,452		
CASES CLOSED	215			$ 5,171,996
NET COLLECTIONS			$ 6,860,324	

Pending at
3/06/90: 9,604 cases with current balance of $136,174,518.

SOURCE: DEPARTMENT OF JUSTICE

ciffy89.90stats

FISCAL 1989

CIF Received:	9,270	backlog debts from USAOs	$ 103,335,588
	1,434	new debts from agencies	43,854,159
	10,704		$ 147,189,747
CIF Referred	7,057	debts to USAOs for	$ 132,923,356
	3,648	debts to private counsel for	14,266,391
	10,704		$ 147,189,747
CIF processed	11,539	payments & deposited net total of cash in Treasury	$ 13,725,679

Pilot USAOs collected	$ 15,791,035
Pilot private counsel collected	$ 174,445
	$ 15,965,480

DoJ paid private counsel contingency fees of $ 49,140 (28.17%).

FISCAL 1990 THRU 2/28/90

CIF Received	1,160	new debts from agencies for	$ 25,725,452
CIF Referred	543	new debts to USAOs worth	$ 22,058,245
	617	new debts to pvt. counsel	$ 3,667,207
	1,160		$ 25,725,452

Pilot USAOs collected (10/1/89 - 2/28/90)	$ 6,181,114
Private counsel collected (10/1/89 - 2/28/90)	$ 451,747
	$ 6,632,861

DoJ paid private counsel contingency fees of $ 104,417 on their collections of $ 451,747, for an average of 23.11%.

SOURCE: DEPARTMENT OF JUSTICE

PRIVATE COUNSEL STATISTICS

DISTRICT/FIRM	DEBTS REFERRED AS OF 4/4/90 NEW	BACKLOG	TOTAL	FY 90 FEES PAID AS OF 3/31/90
E.D. MICHIGAN				
FIRM 1	84	113	197	$ 5,342
FIRM 2	86	114	200	3,502
FIRM 3	91	107	198	9,867
FIRM 4	65	109	174	6,696
TOTALS	326	443	769	$ 25,407
E.D. NEW YORK				
FIRM 1	42	145	187	$ 3,535
FIRM 2	41	141	182	2,669
FIRM 3	40	142	182	3,179
FIRM 4	43	143	186	11,673
TOTALS	166	571	737	$ 21,056
S.D. TEXAS				
FIRM 1	135	298	433	$ 4,209
FIRM 2	134	301	435	5,919
FIRM 3	136	294	430	6,542
FIRM 4	131	301	432	9,921
TOTALS	536	1,194	1,730	26,591
S.D. FLORIDA				
FIRM 1	64	194	258	$ 8,821
FIRM 2	64	191	255	5,780
FIRM 3	61	193	254	18,247
TOTALS	189	578	767	32,848
C.D. CALIF.				
FIRM 1	107	232	339	$ 17,256
FIRM 2	110	223	333	11,335
FIRM 3	108	238	346	8,150
TOTALS	325	693	1,018	36,741
GRAND TOTALS	1,542	3,479	5,021	$ 142,643

Mr. SMITH of Texas. I reluctantly not only have to go, but I reluctantly yield the Chair to my colleague from Kansas.

[Laughter.]

Mr. GLICKMAN [presiding]. Have all the gentlemen on the Republican side had a chance to ask questions yet?

Mr. DOUGLAS. No, I have not.

Mr. GLICKMAN. Mr. Douglas.

Mr. DOUGLAS. Thank you, Mr. Kramer.

One of the areas I am concerned with came out of a hearing we had in Government Operations about a month ago and that concerns the whole trust resolution, OTC, FDIC, S&L mess. I will just think of as many acronyms as I can there. But the bottom line was Justice said that the reason we are not collecting billions of dollars from these various folks who are getting convicted and ordered to pay restitution is that you cannot get blood from a stone. I agreed with that, but I said some of those folks are rats and you can get blood from a rat.

What I am curious is, to what extent would we be better off turning the whole restitution and collection issue for the savings and loan disaster over to the bar on a contingency basis, to let them see if it is the Cayman Islands or wherever the stuff has been hidden, for those who hid it—some just blew it—but for those who hid it, would that not be a better way to go, than having the Justice Department just kind of saying, well, there is not much we can do?

Mr. KRAMER. I agree that it should be in the hands of the professional collector. If the Justice Department can assign enough people who are willing to work as collection attorneys, then maybe that would be the answer, but I do not think that is the best use of their time.

Mr. DOUGLAS. I agree.

Mr. KRAMER. The private sector in the collection industry is used to working on a contingent fee basis and I believe that if you do not burden them with too many problems insofar as compliance with the—I could have done in 4 pages what it took the Justice Department 111 pages. It is because they had to follow certain procedures.

You have a whole collection industry out there just waiting to handle matters and they could handle this well for you, if they were not strapped by a lot of the red tape that governmental agencies create today.

Mr. DOUGLAS. Now, you are not asking for exemptions from debt collection acts or anything like that? You are not talking about statutory requirements about harassing at work and that kind of thing, you are not asking for exemptions from that?

Mr. KRAMER. No, sir. We are bound by the Fair Debt Collection Practices Act.

Mr. DOUGLAS. All right. So, what you are saying is you can live with that act, all you want to do is not live with government red tape, but do it within the law, but on your time, on your watch and your methods?

Mr. KRAMER. I believe we should have the ability to do some negotiating with people, the ability to work pay programs, not be hamstrung by the Government saying you cannot write a letter without our permission. Right now, although we have a pilot project, everything that is done goes through the U.S. attorneys office. There is very little leeway an attorney has in collecting these accounts. In collection, we have to make it worthwhile for the debtor to cooperate. If we have not got a place of employment, we have to be able to bargain a little bit with them. I am not talking about bargaining with the principal, I am talking about with the added charges that are on their interest and penalties, give us permission to do some bargaining.

With an average retail claim, we are handling a matter for 2 years. With an average commercial claim against a firm, it is for 6 months. That is why the figures you are seeing on the pilot project are not accurate, in the sense that you are not seeing the true results of what the private sector can do even with the junk items, because we have only been in it for a few months, even though the law was passed 3 years ago. You are going to see a lot more collected, because it takes time when you work with the consumer.

Mr. DOUGLAS. Let me ask you one last question. If we did privatize it and just, in effect, said Justice has enough to do with prosecuting bank fraud, druggies and everything else, let them deal with that, and when it comes to civil debt collection, we will just privatize that, how much do you think a year you and your industry could bring in to the Government, compared to I guess it was $600 million or something—I have forgotten what the number was Thornburgh said they brought in last year in total, $646 million for fiscal 1989 was the total Justice Department collection—what do you think you could collect?

Mr. KRAMER. Depending upon the amount, I would say that probably at least 17 percent of the older debt. If you are giving us stuff more fresh, then obviously those figures go up greatly.

Mr. DOUGLAS. Everything. In other words, we just say Justice no longer collects money, we privatize that, you are in the prosecution business, you deal with the criminals and, because this is civil, we are just going to privatize it and farm it out to the attorneys on a percentage basis, do you have any guesstimate of what you would be talking about, instead of $600 million, what would it be?

Mr. KRAMER. Well, I do not know what the placement amount is and that is the key.

Mr. DOUGLAS. All right.

Mr. KRAMER. But if you took the placement of claims under $25,000 against individuals, you are probably going to end up with about a 35-percent recovery.

Mr. DOUGLAS. Well, if you get a chance after you leave here, to the extent there are numbers floating around in all the paper that has been passed our way, I would appreciate it, if you do not mind, Mr. Chairman, if he could supplement the record with a letter response of what you think your industry could produce over and above that $646 million.

Mr. KRAMER. Again, the figures in my proposed testimony which is in front of you go all the way up to $32 billion. I do not think anybody that has testified today, even from the Justice Department, really has a handle on what those figures are. The Department of Education indicated you are going to have $2 billion in 1990 in the student loan area, $2 billion of delinquency. I think if that is turned over promptly, you could have 35 to 50 percent recovery, but if it goes beyond 120 days, it is anybody's guess.

Mr. DOUGLAS. All right. Thank you, Mr. Chairman.

Mr. GLICKMAN. Mr. Campbell.

Mr. CAMPBELL. Thank you, Mr. Chairman.

I must appreciate your testimony, Mr. Kramer.

Mr. KRAMER. Thank you.

Mr. CAMPBELL. We seem to agree on a lot of things. I have one or two questions. You heard our colloquy with the previous panel and in that the representatives of Agriculture and Education made what seemed to be a claim of something like this: We know the credit worthiness of the types of claims we deal with and certainly we do in the securities area, so let us have a little bit more discretion to work those out and what we decide, we in the agencies like Agriculture and Education, when we decide that they are not collectable efficiently by our own means, then we, Agriculture and Education, ought to be allowed to sell them to a collection agency. That, at the risk of being unfair, is I think a paraphrase of what they were saying.

That strikes me as sensible. What the present system does, though, is it counts them at $20,000 and for anything more than that requires them to go to the Department of Justice if they are going to go collect, and you have a whole new cadre of attorneys who do not know anything about the case, do not know anything in particular. They know it is for Education or for Agriculture or the collateral involved.

So the divining line I would offer you is that we privatize this, as my colleague from New Hampshire suggests, but at the stage where the agency has decided that they cannot—I mean by the agency, the creditor agency like Agriculture, not the Department of Justice—that we privatize at that stage, when they decide they have not the means to refer them. Now, that would be my cut on the testimony I have heard this morning. I wonder what your response to that division of labor would be?

Mr. KRAMER. I have no quarrel with that at all.

Mr. CAMPBELL. Do you think that there is a role to be played by collection agencies even sooner in an Agriculture or Education program, or would you grant that they have a certain amount of expertise in which ones are collectable quickly?

Mr. KRAMER. I think, in the first place, collection agencies have to be given an incentive to work on it. When an agency bids 4 percent for the handling of items, you can imagine what they are going to do for 4 percent, and you had competitive bidding that ran from 4 percent to 29 percent. They have to be given an incentive.

In the second place, they do not have the right to sue or turn it over to an attorney, so their progress is very limited. I think most of the agencies handling this previously probably have not made money, if at all, in this program. I do not know how interested agencies will be. There are certain types of agencies that would be very interested in your claims under $500, and you may have 50,000 of those that have never even received a letter, so that is an area you may want to consider.

The agencies have a great value. There are some fine agencies who could handle it, but they need the ability to work with attorneys when they cannot handle it. They cannot threaten suit, because they cannot follow through with it.

Mr. CAMPBELL. One last question. I appreciate the chairman's patience with me. Selling debt versus farming out of debt is a distinction of great importance here. I will tell you what I prefer and then I want to ask you, Mr. Kramer, what the real world is.

I prefer to get this whole business out of the departments entirely, get as many dollars to the U.S. Treasury as possible, as quickly as possible, and let somebody else go collect. I am half suspicious that nobody would bid on selling debt, that most of the activity that with which you are familiar, and you can inform us about, is taking a percentage on whatever is collected as a contingency, but I thought I would ask anyway. Is there a market out there just to sell the debt outright?

Mr. KRAMER. There certainly is a market, but that market is remarkably small, compared to what you could get through other sources. If you will check with the credit card companies and see what they are selling credit card debt, new credit card debt is going for like 11 cents on the dollar. Old credit card debt is going like 3.5 cents on the dollar. Right now, the debt by the time it gets out of Federal Government agencies is all old debt, so you are going to get a very low bid, if there is enough money in the private sector to buy all those accounts.

Mr. CAMPBELL. Thank you very much, Mr. Chairman.

Mr. GLICKMAN. I do not really have any questions. It is kind of ironic that I am sitting here, because I was the author of the bill which passed the House which provided the pilot programs. I was Mr. Franks' predecessor in this position.

I remember a couple of things we went through during that bill. One is that there were some scandals involving debt collection and private attorneys, primarily in New York City, and we were very careful about drafting the legislation so as to not get the Government involved in any preferential arrangements with attorneys. We are still concerned about that, so we drafted the bill to prevent that from happening. It looks as if the Department of Justice has taken seriously that concern and others so related. They have dragged their heels really on doing anything in this area and that concerns me.

Mr. Campbell, your use of the term "farming out" brought to mind a policy concern. In some areas Congress has exhibited an intent not to have its debts collected at all, as a matter of policy, and one of the areas is agricultural loans, where we have put moratoria on collection. One of the public policy issues here is that if we are rather indiscriminate in having debts collected through private sources, then the Government loses its policy control over what debts it does and does not want to pursue zealously. That is just a practical aspect of this that we deal with all the time.

Mr. KRAMER. One of the things I deal with in my proposed testimony is the fact that if you do not want to foreclose on 100,000 farmers, I understand that, but at least let us press them for some payments.

Mr. GLICKMAN. Surely.

Mr. KRAMER. One thing is a moratorium, I do not know, maybe they are pressing them, but at least do not make a moratorium on their paying on a note secured by a mortgage or a security agreement on a piece of property. You could still collect on the note.

Mr. GLICKMAN. Well, I guess what I am saying is if we choose not to do that, we ought to write into a statute that you shall not use this law to collect farm debts, period, and we could not do that. That is just a matter of public policy that Congress would have to decide.

I am intrigued with Mr. Douglas' point, however, that when I go home, the one question people ask me is, "Where is the money?" The money they are talking about is the money that has disappeared in the savings and loan situation. It is very hard to give people an articulate explanation of where did it go, did it evaporate? Is it in some yacht? Some fraud scheme somewhere? So, I am kind of intrigued by the idea of letting this debt collection process work to collect on mismanagement in the savings and loan industry.

I want to see these pilot projects work. I have thought that they have been set up in districts which are not necessarily indicative of the population as a whole. They have almost decided to have their pilot projects in districts that would be almost impossible to get a program working well.

Mr. KRAMER. When the first five pilot districts were selected, I called the Justice Department and said why did you pick them, because Florida, Texas, and California are traditionally extremely hard to collect in—their laws are not very favorable for collection—and the other two areas, Brooklyn and Detroit were also tough areas. And the answer was, well, we picked the areas that it is toughest for the U.S. attorney to collect in. I said what kind of a pilot is that? You picked all tough areas. Why don't you see how the pilot will work in an easier area? So you are right, they are using it to try and figure out how to collect in the tough areas.

Mr. GLICKMAN. I think there was institutional reluctance on the part of the Department of Justice to see this program work. I think that is basically what we have.

Mr. KRAMER. And again——

Mr. GLICKMAN. I hope we are able to extend this and then perhaps look at some of the other ideas. I would finally mention that we have a bill going through this committee, an alternative dispute resolution, which has as its goal the encouragement of settlements without having to go to court in certain circumstances on a voluntary basis. We note that in one of these bill reforms there is some mention of a higher amount the Attorney General is permitted in terms of settlement without having to take a case to court and this kind of thing, which is another concept.

We appreciate very much your testimony.

Mr. DOUGLAS. Mr. Chairman, one thing that amazes me, and I read it and I missed hearing it live, is that the Justice Department attorneys do not even want to do this stuff, so the irony is they are trying to hold onto something they all hate doing anyway, and that has always been one of the great——

Mr. GLICKMAN. In my judicial district, which is an easier collection district, I find that there is a fairly active collection effort on the part of the Justice Department attorneys. It depends, I guess, on where you are from and we are an honest area, we have less crime.

Mr. DOUGLAS. You have to do something.

[Laughter.]

Mr. DOUGLAS. OK. We thank you very much and I assume that is the last witness today. We appreciate your testimony.

Mr. KRAMER. Thank you.

Mr. GLICKMAN. The hearing is adjourned.

[Whereupon, at 11:45 a.m., the subcommittee adjourned, to reconvene subject to the call of the Chair.]

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